CG WATCH 2023

GREATER CHINA

Edging up, sliding down

Top-down agendas, contrasting outcomes

Special report - August 2024

Founding Sponsor of ACGA

Jane Moir
Head of Research, ACGA
jane@acga-asia.org
+852 2160 1797

Lake Wang
Research Manager, ACGA
lake@acga-asia.org
+852 2160 1785

Stephanie Lin
Research Manager, ACGA
stephanie@acga-asia.org
+852 2160 1798

Jamie Allen
Former Secretary General, ACGA

Building on the insights in the full CG Watch 2023: A new order

Contents

Executive summary ... 3
CG Watch through the years ... 4
China - Adapting to national priorities ... 5
Hong Kong - Walking a tightrope ... 32
Taiwan - Holding its own and improving ... 65

All prices quoted herein are as at close of business 30 July 2024, unless otherwise stated

Click to rate this research

Great

Solid

Meh

Disclaimer

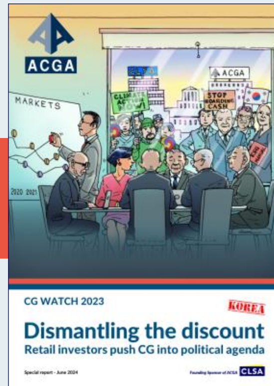
This is not investment analysis of securities and this is not investment analysis of factors likely to influence the future performance of securities.

This document is for information purposes only and is not a solicitation or any offer to buy or sell. The contents of this document were not verified by CLSA nor approved by the relevant company. CLSA does not guarantee and makes no representations as to its accuracy, completeness or correctness. We expressly disclaim all warranties and liabilities, express or implied of any kind relating to this publication.

You should make your own independent evaluation of the relevance and adequacy of the information contained in this document and make such other investigations as you deem necessary, including making enquiries with the company and obtaining independent financial advice. You shall not rely on the contents under this document for securities investment purposes, otherwise you shall be solely responsible if you suffer any losses.

Copyright of this publication/communication belongs to ACGA and the provider(s) of relevant information included hereof. Neither the publication/communication nor any portion hereof may be reprinted, sold, resold, copied, reproduced, distributed, redistributed, published, republished, displayed, posted or transmitted in any form or media or by any means without the written consent of ACGA and/or its affiliates.

Take the regional view



CLSA and CL Securities Taiwan Co., Ltd. ("CLST") do and seek to do business with companies covered in its research reports. As such, investors should be aware that there may be conflicts of interest which could affect the objectivity of the report. Investors should consider this report as only a single factor in making their investment decisions.

Find CLSA research on Bloomberg, Thomson Reuters, FactSet and CapitalIQ - and profit from our evalu@tor proprietary database at clsa.com

For important disclosures please refer to page 101.

Edging up, sliding down

Taiwan leads the pack followed by Hong Kong and China

The trajectory of corporate governance in the Greater China region is a story of modest gains, stability and some areas of slippage since our last CG Watch in 2020. Of the three, Taiwan is the only market to have moved up in our rankings, gaining a spot to place equal 3rd with Singapore. China maintained its 10th position with a slightly improved score, while Hong Kong dropped four places to rank equal 6th with India, a notable change for the market typically found among the top three.

Click to rate this research

Great

Solid

Meh

All three are rules-driven markets although outcomes vary

A common factor among the three is the influence of rules in setting the overall CG tone. Taiwan policymakers are consistent in seeking to deploy governance to bring itself closer to global investors, yet its government-driven system maintains legacy issues and box-ticking corporates sometimes struggle to keep up. Hong Kong maintains a solid rulebook in protecting investors, albeit still lacking recourse such as class actions, but its recent focus on IPO volume has come at a cost to minority investors. China's self-sufficiency drive as it decouples with the West, and the US in particular, largely leaves CG ancillary to capital market aspirations but has provided a few bright spots (INED reform in particular) as the quality of domestic enterprise comes into sharper focus. Elsewhere, progress is patchy.

Investors and civil society contribute to mixed degrees

The other cogs in the CG machine, such as investors and civil society, meanwhile provide varying degrees of support to the overall ecosystem. Taiwan again is stronger here, with a vibrant civil society and media: there are even a few hints of shareholder activism. Hong Kong has taken a tumble in this category yet maintains solid options for director training (even if corporates do not always bite). Activism is rare, and majority control at corporates prevails. In general, domestic investors keep under the radar in the region, the foreign contingent remaining the more active stewards.

Taiwan moved up the rankings; Hong Kong drops

CG Watch 2023 market rankings and scores (%)

Market	Previous ranking	2023	2020	Change vs 2020 (ppt)
1. Australia	1	75.2	74.7	+0.5
2. Japan	=5	64.6	59.3	+5.3
=3. Singapore	=2	62.9	63.2	-0.3
=3. Taiwan	4	62.8	62.2	+0.6
5. Malaysia	=5	61.5	59.5	+2.0
=6. Hong Kong	=2	59.3	63.5	-4.2
=6. India	7	59.4	58.2	+1.2
8. Korea	9	57.1	52.9	+4.2
9. Thailand	8	53.9	56.6	-2.7
10. China	10	43.7	43.0	+0.7
11. Philippines	11	37.6	39.0	-1.4
12. Indonesia	12	35.7	33.6	+2.1

Source: ACGA

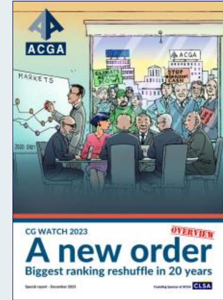
CG Watch through the years

Saints & sinners
April 2001

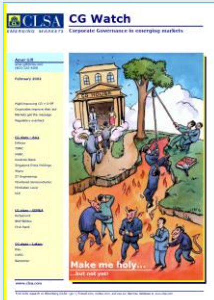
The holy grail
October 2005

Dark shades of grey
September 2014

A new order
December 2023



Make me holy . . .
February 2002



On a wing and a prayer
September 2007

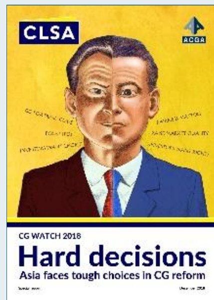
Ecosystems matter
September 2016

Ramping up CG reform
May 2024

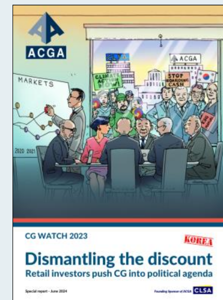
Fakin' it
April 2003

Stray not into perdition
September 2010

Hard decisions
December 2018



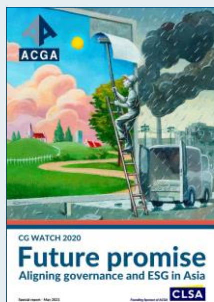
Dismantling the discount
June 2024



Spreading the word
September 2004

Tremors and cracks
September 2012

Future promise
May 2021



Spectrum of standards
June 2024

Lake Wang
Research Manager, ACGA
lake@acga-asia.org
+852 2160 1785

Stephanie Lin
Research Manager, ACGA
stephanie@acga-asia.org
+852 2160 1798

Jane Moir
Head of Research, ACGA
jane@acga-asia.org
+852 2160 1797

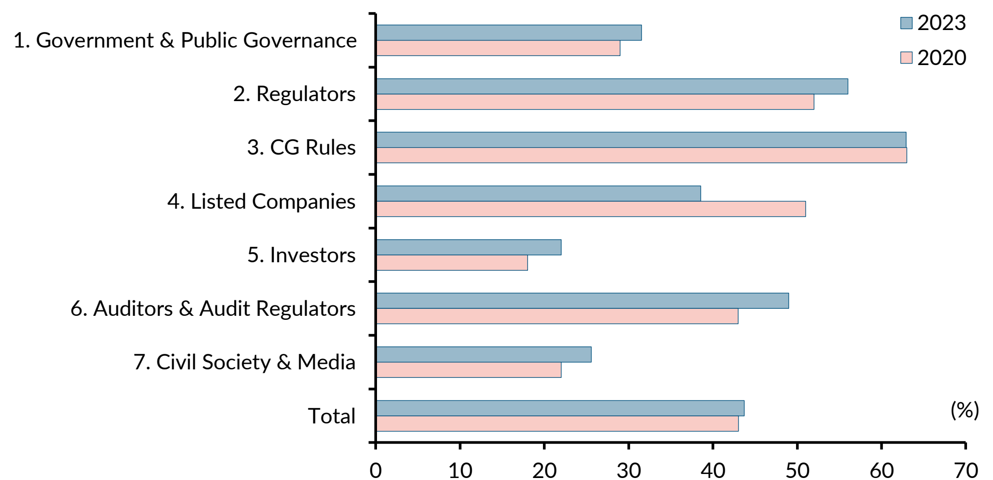
China - Adapting to national priorities

- China remains in 10th place with a score of 43.7%, a marginal 0.7% increase on its 2020 performance
- State objectives to promote strategic industry, national security and common prosperity take priority and CG upgrades are piecemeal, but the quality of listed companies and valuations come under increased scrutiny
- The CSRC takes control of the offshore IPO pipeline, and the role of Party Committees is fortified in company law and further embedded in corporates
- Revamped rules on independent directors clarify roles, duties and qualifications and increases supervisory powers
- Still no stewardship code but renewed vigour from regulators encourages greater investor involvement in CG - and a mandate for SOEs to be more communicative with shareholders
- No improvement in listed company disclosure and longstanding issues prevail, including the lack of independent chairs, poor visibility on executive remuneration and few women on boards
- Retail activism is patchy, but class action-style lawsuits are gaining momentum and hefty fines are levied by the courts on bad actors
- China still lacks an independent audit body but regulators have stepped up inspections and sanctions

Click to rate this research

Figure 1

China CG macro category scores: 2023 vs 2020



Source: ACGA

China remains in 10th place on a score of 43.7%

Introduction

A shift in national priorities since our last CG Watch in 2020 has largely driven the CG agenda in China, as capital markets policy falls into step with evolving economic and industrial ambitions. This has played out against the backdrop of a challenging geopolitical landscape. Some incidental CG gains have been made - revamping the independent director regime was a welcome step, as is the state edict for SOEs to become better communicators with their shareholders and a focus on better valuations. But these are intermittent moves, and the CG agenda remains on the periphery as the PRC pursues an economic policy with technological self-

sufficiency and national security at its nexus. It has been a rollercoaster few years, from lockdowns and restrictions during the Covid pandemic, turmoil in the financial and property markets and structural tensions between China and the US. Geopolitical risk is a prevalent concern among foreign investors as both sides take a harder line on inward and outward investment to their markets. Longstanding issues endure and leave China once again stuck in 10th place in our survey on a score of 43.7%: China has consistently remained in the same territory in terms of both score and rank for the past decade.

Gains were had in five out of seven categories

China gained ground in five out of seven categories, with its strongest performance found in the enforcement sub-category. Regulators have shown a robust appetite to tackle the abysmal financial performance of "zombie" companies by taking them off the exchanges with renewed vigour. They have also been meting out more penalties for market misbehaviour. Progress was however less evident in the CG Rules category where China's score remained flat as other markets moved faster in improving their frameworks. Still, an overhaul of the independent director regime - notably giving clarity on directors' roles and powers - was a bright spot.

Listed companies still score badly on disclosure but are encouraged to engage

In other categories, it was a mixed story. Listed companies failed to invigorate the CG ecosystem with their disclosure which remains a reflection of what regulators require of them and little else. An uptick in score was found in the Investors category, although China remains second-last, behind Indonesia. Regulators are on paper encouraging greater investor involvement in CG, notably promoting more "proactive" discourse with corporates. ACGA has seen some issuers more willing to engage and share, particularly the large state-owned firms.

Minority shareholders are taking bad corporate actors to task

Shareholder activism is still rare: retail investors are not big voters, with just over 5% exercising this right. But it was refreshing to see the momentum on class actions continue after the landmark Kangmei Pharmaceutical case in late 2021 resulted in a hefty RMB2.46 billion (US$340m) payout to investors who suffered from a massive fraud at the company. Although these actions are undertaken by a non-profit set up under the direct administration of the securities regulator, they can pack a punch in financial terms and put delinquent directors in the spotlight.

Still no audit oversight body but some focus on quality control

There was improvement in the Auditors & Audit Regulators category, although China still ranks 12th. While there is no independent oversight body, quality control has been an area of focus as the government seeks to address shortcomings of audit firms as gatekeepers, and inspection frequency was stepped up at larger firms. China comes last in the category of civil society & media, although its score improved marginally based on improvements in the quality of director training on offer and the efforts of some organisations in raising CG awareness.

Recapping CG Watch 2020

Some recommendations from CG Watch 2020 have been adopted

We made several key recommendations in our 2020 CG Watch. China has made progress on some fronts, notably ESG disclosure guidance for companies, as the table in Figure 2 shows:

ESG guidance is a recent area of progress

Figure 2

China: recap of 2020

	Recommendations	Outcomes
1.	A clear direction from government on CG improvements.	The CG agenda remains intermittent as national objectives evolve.
2.	The stock exchanges could make annual disclosure on budgeting.	No progress.
3.	More detailed regulatory announcements on enforcement cases.	No substantial changes in disclosure.
4.	Do not amend the Company Law to allow for dual class shares across the board	Amendments to the Company Law in December 2023, effective from 1 July 2024, allowed unlisted companies to issue dual-class shares.
5.	Greater ESG disclosure guidance for companies	China introduced guidelines in February and May 2024.

Source: ACGA

1. Government & public governance

China scores 32% and remains in 10th place

China scored 32% in this category, which represents a three percentage-point increase from 2020. It remains in 10th place, as it did in our last CG Watch. There were marginal increases, notably in the question we ask about the direction of overall CG strategy. Otherwise, scores on all other questions remained flat.

There has been a residual policy focus on CG

We bumped up China's score by one point to two out of five on our question as to whether the government has a clear and credible long-term strategy to promote CG reform to support capital market and business development. CG may not be at the forefront of the state's agenda, but national policy to develop the capital market and improve the quality of issuers has had a residual impact. This is in a landscape where national security and strategic industries are paramount, and CG pivots around these goals. Still, policymakers have made it clear they wish to unlock value in state firms and address low valuations. The CSRC's three-year action plan (2022-2025) to improve the quality of listed companies does mention CG as part of its commitment to upgrade state-owned entities and strengthen returns. In November 2022 then CSRC chair Yi Huiman floated the notion of a "valuation system with Chinese characteristics" along with a call to issuers to boost their "core competencies" and strengthen their investor relations. The comments, and commitment to improve competitiveness at SOEs did cause a rally in PRC stocks but convincing investors not to discount these state giants requires substantial change in how they operate. We incorporated changes to the IPO registration system in our scoring, which saw the system expanded from the smaller Star and ChiNext boards to include the main Shenzhen and Shanghai bourses.

National priorities have shifted

The overarching story of the past few years has however been the consolidating of Party control at state and corporate level as the national leadership charted a new course distinct from their predecessors. Pursuit of the national agenda has taken priority over the more liberal aspects of capital markets and some corners of private enterprise have seen their wings clipped. As we left off in our last CG Watch in 2021, the China tech crackdown was just beginning to bite, with the aborted IPO of Jack Ma's Ant Group one of several casualties resulting from tighter regulatory scrutiny of internet giants. Ma's Alibaba in September 2021 received a record RMB18 billion (US$2.8 billion) fine for antitrust violations and the competition regulator, the State Administration for Market Regulation widened the net to other internet and new economy peers, including Tencent and ride hailing app Didi. Then came the abrupt demise of the vast private education sector in July 2021 as Beijing banned after-school tutoring. In June 2021, it emerged that the IPO of Didi in New York went ahead against the wishes of PRC regulators who were concerned about

data security and less than six months later it pulled the plug and announced plans to delist. Investors perceived an increased political risk of investing in Chinese companies, and the tech sector took a beating. Offshore IPOs saw a near freeze as Chinese firms shelved ambitions to list in markets such as New York.

A crackdown on big tech and new rules on offshore IPOs takes a toll . . .

As we reported in late 2021, decisions by the state to take token stakes in key entities of mainland tech giants such as ByteDance and Weibo underscored a tactical shift toward more direct influence on private enterprise. The regulatory playbook of curbing the influence of tech giants did little to quell investor anxiety as boundaries between state-owned and private firms became increasingly blurred. At the same time, the China Securities Regulatory Commission (CSRC) brought offshore listings under its direct control in February 2023 with the "Trial Administrative Measures of Overseas Securities Offering and Listing by Domestic Companies": while the revised approval process paved the way to resume IPOs in markets such as Hong Kong and New York, obtaining the green light to list has become contingent on the nature of the business and whether it aligns with Beijing's economic priorities for capital-raising on foreign markets, as well as data security clearance. This includes whether a company has requisite safeguards against revealing considered state secrets. Meanwhile, Chinese state-owned enterprises in the US packed their bags: there are now no Chinese SOEs listed on US exchanges.

. . . but a new domestic IPO regime streamlines listing applications

Changes to the IPO regime also came into force for domestic listings, and in February 2023 the CSRC released the "Measures for the Administration of Initial Public Offering Stock Registration" setting out requirements for listings on the Shanghai Stock Exchange (SSE) and Shenzhen Stock Exchange (SZSE). The new regime represents an expansion of the IPO registration system initially piloted at the smaller Shanghai STAR market in 2019 and the ChiNext board in 2020. In 2021 the same system applied to the new Beijing Stock Exchange, announced by President Xi Jinping in September that year, as the primary platform for booming tech SMEs, upgrading the old National Equities Exchange and Quotations (NEEQ). Trading on the new exchange began on 15 November 2021. In April 2023, the first companies began trading under the new IPO regime. Companies would no longer need prior approval from the CSRC to list, a requirement long seen as impeding the frequency of listings. A streamlined system put the task of reviewing IPO candidates in the hands of stock exchanges, with the CSRC taking a supervisory role most notably to review whether companies comply with national industrial policy. The rules also put a time limit of three months for the exchange to respond to an application. The CSRC no longer determines the price of shares: instead, it stated that the market should play a decisive role in valuing companies. Ultimately however the government still favours companies in strategically important sectors to tap the capital markets, limiting the overall freedom of companies to list.

A new 'super' regulator and changes of the guard

A new national financial supervisor is established

China's financial supervisory infrastructure saw an overhaul in May 2023 with the establishment of the National Financial Regulatory Administration (NFRA), which sits directly under the State Council. In what was seen as a restructuring to exert greater control in the oversight of China's myriad and complex banks and other financial institutions (including shadow banks), the NFRA replaced the old China Banking and Insurance Regulatory Commission (CBIRC) and took over some of the functions of the People's Bank of China (PBOC) and the CSRC. The PBOC would focus more on monetary policy and macro supervision, with the NFRA taking over financial consumer protection from the CSRC, which is elevated to a "government

agency" directly under the State Council as part of the restructuring. In December 2023, Li Yunze, director of the NFRA, said there would be greater reform of small and midsize financial institutions, to deal with "key people" and "key behaviours" causing financial risk.

New faces head up the CSRC and PBOC

People movements at both the CSRC and PBOC meanwhile have underscored national priorities within the capital markets, with the decision to appoint 58-year-old Wu Qing as chairman of the CSRC on 7 February 2024 seen as a more determined effort to address a market rout and boost market confidence. Wu replaced Yi Huiman and had a reputation as a hardliner on bad behaviour: his nickname as the "brokerage butcher'' was acquired after a previous stint at the regulator when he shuttered 31 brokerages for violations during the mid-2000s (this was about a quarter of all securities firms at the time.) Wu came to the CSRC from the Shanghai Stock Exchange and spent two years as a deputy in Shanghai's municipal government. And in July 2023 People's Bank of China (PBOC) governor Yi Gang was replaced by Pan Gongsheng, the deputy governor. Yi had been seen as a liberal force within the PBOC, a US-trained economist who was viewed as modernizing monetary policy.

Party committees fortified

Company law rewrite solidifies role of the Party

A rewrite of China's Company Law took place in the latter part of 2023 and the changes were effective 1 July 2024. Although the overhaul took place after we completed our scoring, one notable feature - a new section on the regulation of state-funded companies - is worth highlighting as it solidifies in law the scope of Party Committees not just in SOEs but in firms where the state has a controlling stake (China's company law defines this as at least 50% in shareholding terms or where voting rights can enable majority control). The new section requires Party organisations within these firms to play a leadership role and "deliberate and discuss major business management matters of the company and support the company in exercising its powers in accordance with the law.''

Details of how Party Committees interact with boards is still a black hole

Investors hoping for more transparency in how Party leadership in listed companies plays out in practical terms would however be disappointed. Disclosure on the work and impact of the Party Committee within firms remains elusive. When ACGA conducted research on the top 100 listed companies in China during 2023 to analyse gender diversity on boards, very little information was available from annual reports on the how these committees operate and interact with senior management in the decision-making process. A handful of large SOEs in the top 50 were opaque on the presence of Party Committees: seemingly embedded in the company, there is no sign of issuers giving shareholders transparency on their actions and working relationship with the board. Still, if the view taken by the Party on some of these issuers is anything to go by, SOEs are falling short of full conformity with what is expected of them in terms of adhering to the Party line. The largest SOEs are inspected by the Party and in September 2023 a review of 30 centrally administered SOEs noted "prominent problems''. One on one feedback with the Party Committees in these companies highlighted failures to fully implement CPC Central Committee decisions, and weak adherence to Party governance.

Anti-corruption drive escalates in the finance sector

Graft probes gain momentum in the finance sector

China ranks 76th out of the 180 countries tracked in Transparency International's Corruption Perceptions Index (CPI) on a score of 42, a decline from 2022 when it scored 45. The Central Commission for Discipline Inspection (CCDI) of the Party brought the financial sector into focus in late 2021. CCDI began an inspection of more than 20 institutions, such as the central bank, stock exchanges, commercial banks and asset management companies at this time.

Several high-ranking officials are under investigation

Macroeconomics research firm Gavekal reports that 75 cases were announced in 2023 involving officials at these institutions and financial regulators, including high-ranking ones: there were eight such probes during the year, compared to two in 2022. Bank of China chairman Liu Liange was sacked in 2023 following a CCDI probe and in February 2024 he was indicted on charges of bribery related to his position at the lender and previously as president of the Export-Import Bank of China. In March 2024, the former chairman of state-owned Bank of Beijing Yan Bingzhu came under investigation for "seriously violating discipline and the law." He retired as chair in 2017. And in May 2024 Ren Chunsheng, who had barely started a senior role at the National Financial Regulatory Administration (NFRA) was reported to be under investigation by the CCDI. In January 2024 President Xi said he would intensify the anti-corruption campaign in the finance, energy, pharmaceutical and infrastructure sectors, areas where "power is concentrated, capital is intensive, and resources are rich."

2. Regulators

China moves up to 8th place with a score of 56%

China's score increased four percentage points to 56% and it moved up a place to rank 8th. Scores for both sub-categories we have in this section improved, with Enforcement being the biggest contributor as we saw more enforcement outcomes by the CSRC. It imposed more administrative penalties, and the stock exchanges delisted a record number of poor-performing "zombie companies" and "black actors". The higher score was also due to regulatory amendments to the listing rules in response to the full implementation of the registration-based IPO system. But China still scored poorly on questions related to public consultations, disclosure of funding and staffing by its stock exchanges, and the conflict of interest between the political and supervisory roles of the regulator. Lastly, there was a wide discrepancy between the provision of Chinese and English disclosure on regulatory websites.

2.1 Funding, capacity building, regulatory reform

China stays in 10th place on an improved score of 44%

China's score increased two percentage points to 44% in this sub-category, although its ranking remained the same at 10th. On funding and capacity building, the CSRC is reasonably transparent in disclosing its budgets, although there are some gaps over income sources. The funding picture at the two major exchanges meanwhile remains opaque.

Funding for the CSRC has increased materially despite a budgeting mistake

In 2021 the CSRC disclosed a budget of RMB1.21 billion in its annual budget planning report. But the National Audit Office discovered in 2022 that this figure did not include RMB530m of financial subsidies from local governments. As a remedy, the securities regulator incorporated these subsidies into its 2022 budget report, which consequently ballooned to RMB2 billion. The size of budgets then increased at an accelerating speed to reach RMB2.2 billion in 2023 and RMB2.8 billion in 2024.

The securities regulator is receiving less from the central government

The bulk of the CSRC's budget is funded directly by the central government. In 2022, nearly three-fifths of the budget was financed by fiscal allocation from the central government, over one quarter from "other income", and the remainder from surpluses and carryover funds. The following year, the proportion of the central budgetary allocation fell slightly to 56% while that of "other income" rose to 27%. A similar pattern emerged in 2024: less than half of the budget was from the central coffers while nearly one-third from other income sources.

"Other income" remains a mystery

The CSRC's disclosure on "other income" is scant. The 2021 budget planning report did shed some light on the sources of "other income", which "mainly include rental income, term deposit interests, and so on". But this piece of information was nowhere to be found in the subsequent budget reports.

The CSRC has heavy administrative costs

In terms of budget allocation, the CSRC spent more than two-thirds of the total budget on maintaining its daily operations and administrative functioning. Surprisingly, the combined proportion of the budget allocated for enforcement and investigation shrank from 12% in 2021 to 8% in 2024, despite a modest increase in dollar amounts. Meanwhile, spending on IT systems accounted for less than 1% of the total budget. The ratio of the training budget was even lower at 0.1%.

Figure 3

CSRC's key budget items[1]

(Rmbm)	2021	2022	2023	2024
Administrative operation	**1,150** (66%)	**1,267** (62%)	**1,463** (65%)	**1,711** (61%)
Enforcement	**152** (9%)	**156** (8%)	**164** (7%)	**169** (6%)
Investigation	**50** (3%)	**54** (3%)	**61** (3%)	**59** (2%)
IT & Technology	**9.8** (1%)	**7.9** (0.4%)	**8** (0.4%)	**12** (0.4%)
Training	**1.6** (0.1%)	**1.6** (0.1%)	**1.9** (0.1%)	**1.5** (0.1%)
Total budget	**1,750**	**2,045**	**2,247**	**2,807**

[1] We use actual spending figures for 2021 given the budgeting mistake. Source: CSRC, ACGA analysis

The CSRC spends more on allowances than basic salaries

Staff numbers increased from 3,376 in 2021 to 3,590 in 2022. Budgets for salaries and allowances rose steadily between 2021 and 2024, with bonuses peaking in 2022. Interestingly, the budget for allowances comfortably exceeded that for salaries during this period. The CSRC's staff historically received higher pay than civil servants. But in March 2023, the CSRC became a government agency, rather than a public service unit (shiye danwei), directly under the State Council. As a result, its staff may face pay cuts as they are now treated as public servants.

Figure 4

CSRC's staff numbers and key budget items for human resources[1]

(Rmbm)	2021	2022	2023	2024
Salaries	105	120	139	145
Allowances	378	420	436	464
Bonuses	7.9	13	11	12
The number of staff	3,376	3,590	na	na

[1] The figures include salaries, allowances, and bonuses allocated for the CSRC's branch offices. We use actual spending figures for 2021 given the budgeting mistake. Source: CSRC, ACGA analysis

The main stock exchanges are opaque on budgets and staffing

In contrast to the CSRC, the Shanghai and Shenzhen stock exchanges no longer disclose any budgetary data, although both publish lengthy statistical reports on market developments every year. This was not always the case. Both disclosed broad brush numbers on staffing and salary expenditure for 2019-2021, citing a 2018 directive from the State Council which mandated state-owned enterprises to disclose total and average staff salaries. In 2021, for example, the Shanghai Stock

Exchange (SSE) paid RMB1.27 billion in salaries to 2,158 employees while the Shenzhen Stock Exchange (SZSE) spent RMB1.3 billion on salaries for around 2,500 staff. This disclosure appeared to be voluntary since the two exchanges are, strictly speaking, not state-owned enterprises. No such information has been provided from 2022 onward.

Regulatory reform

INED reform defines roles and powers

There have been some areas of reform which could benefit board quality. The State Council in April 2023 kickstarted improvements to the independent director regime with high-level opinions on steps to be taken, with the CSRC following through in August that year with specific measures: most notably a tighter definition of an independent director and the supervisory powers underscoring the role. The new measures beefed up the credentials required of INEDs, that they have at least five years' experience in law, accounting, economics or other relevant professions. At the same time, issuers are expected to give these independents sufficient remuneration, resources and other support to fulfil these functions. There is also a requirement that at least half the members of audit, nomination and remuneration committees comprise INEDs. An enhanced governance structure became a possibility - at least on paper.

The securities regulator has beefed up requirements in other areas

Other improvements have seen the CSRC in June 2021 revise content for annual reports, requiring issuers to provide more granularity on how directors perform their duties and to disclose the content of board committee meetings. The regulator in April 2022 issued guidelines requiring companies to improve their investor relations practices; in January 2022 the regulator enhanced company monitoring of insiders; and in February 2023 specific limits were placed on non-pre-emptive issuances (see our section on CG Rules).

In November 2022, the CSRC introduced the "Three-Year Action Plan for Improving the Quality of Listed Companies (2022-2025)." This plan outlined key tasks and strategies in eight areas, some of which overlapped.

- **The "quality of rules":** The CSRC would address loopholes and revise outdated rules. The Plan highlighted the importance of the long-awaited "Regulations on the Supervision and Administration of Listed Companies", considering it the foundation of the CSRC's future rule system. The State Council stated in its 2024 legislation plan that it would undertake preparatory work for the regulation in 2024.
- **Addressing "deep-seated corporate governance issues":** Key measures included strengthening rules for independent directors, encouraging institutional investors to participate in CG, and requiring listed companies to enhance investor communication.
- **Information disclosure:** Sustainability reporting rules would be developed based on "practical situations" in China. Moreover, listed companies would be required to eliminate unnecessary information and highlight "key information" when making disclosures.
- **The composition of listed companies:** The CSRC would facilitate the listing of "high-quality companies" while delisting poor-performing companies from the market.

- **"Stable" development of companies and capital markets.** Issuers would be encouraged to "focus on their core businesses and make prudent investments". Additionally, the CSRC will attract more "long-term capital" (eg, pension funds, insurance companies, banks) into the stock market.
- **Enforcement actions on "major violations of law":** Three key enforcement areas included share sale fraud, financial fraud, and the misappropriation of funds.
- **Enforcement capabilities.** The Plan stressed the need to create "a regulatory toolkit" without elaborating on any concrete measures.
- **Collaboration with stakeholders.** The CSRC would work with other government agencies and local governments to enhance the quality of listed companies. Moreover, the importance of accounting firms, brokers, and other intermediaries as gatekeepers was also highlighted.

SOE reform: buzzwords vs reality

SOE reform suffers from style over substance concerns

Reform of state enterprises completed a three-year cycle in January 2023, concluding the process a resounding success. At a high level the next round of reform is focussed on "core competitiveness and functions of SOEs,'' which includes strengthening the role these behemoths play in national strategy. There has been some progress on enhancing the metrics used to evaluate these companies. In March 2023 the State-owned Assets Supervision and Administration Commission (SASAC) announced tweaked performance metrics for its largest SOEs to include operating cash ratio and return on equity. More emphasis was put on profitability and cash flow of new investments, as well as risk controls with the goal of SOEs setting their sights on stable net debt/asset ratios. Vowing to benchmark SOEs against global peers in terms of value creation, the stock market improved initially - but much of the hubris around these moves (regulators coined the catchphrase a "valuation system with Chinese characteristics") has been dampened by the view that policymakers are attempting to talk up ailing capital markets. The government in February 2024 then requested state firms to benchmark SOE management against stock market performance.

Company law reform

So long to supervisory boards?

China's company law received a substantial overhaul during our CG Watch scoring, although the outcome of the revisions was only confirmed after we had concluded the process. As we have reported, a notable change is that issuers may ditch supervisory boards in favour of an audit committee, although companies opting to take this route will still be required to have an employee representative on the board. The audit committee would have to comprise at least three members, half of whom could not have any position in the company except that of director. This seems a significant departure from the two-tier board system, where the board of directors runs in parallel with a supervisory board. But it may be a pragmatic one, given the limited oversight function that the supervisory board has in practice, adding little value to companies.

Climate reporting rules with Chinese characteristics

Climate reporting guidance is finally issued

Long-awaited guidance on ESG reporting landed in February 2024, with issuers given a roadmap - following the TCFD model - in how to report on climate and sustainability, with caveats that social factors play a hardy role in this process. And in May 2024, China gave an indication of the degree to which it would adhere to the global ISSB standards with the release of a draft sustainability disclosure framework by the Ministry of Finance (MOF) The draft, titled "Corporate

Sustainability Disclosure Standard - Basic Standard", largely follows the structure of IFRS S1, outlining sustainability disclosure requirements in four key areas: Governance, Strategy, Risk and Opportunity Management, and Metrics and Targets. The key deviation from IFRS S1 is on materiality. While IFRS 1 focusses on financial materiality, the draft standard takes a page from the European playbook to adopt the concept of double materiality. Other main differences can be found in Figure 5:

Figure 5

Main differences between the MOF's draft standard and IFRS S1

	MOF's draft standard	IFRS S1
Materiality	Financial materiality and impact materiality	Financial materiality
Primary users	Investors, creditors, government agencies and other stakeholders (eg, employees, customers, suppliers, business partners)	Existing and potential investors, lenders and other creditors
Location of disclosures	A standalone sustainability report	Within general-purpose financial reports
Time horizons	The time horizons are defined as follows: ❑ Short term: within one year after the sustainability reporting period ❑ Medium term: one to five years after the reporting period ❑ Long term: more than five years after the reporting period. Companies can develop their own definitions of medium and long-term horizons if they are in special industries or have unusual operating cycles and investment horizons.	Companies have the discretion to define the time horizons - short, medium, and long-term - over which the effects of sustainability-related risks and opportunities can be reasonably expected.

Source: Ministry of Finance, IFRS Foundation

VIEs . . . implicit tolerance?

More transparency on funding for stock exchanges

For years investors have kept one foot on the ground in respect of offshore listed entities using a VIE (variable interest entity) structure. Chinese regulators have never officially sanctioned the use of VIEs, which enable companies such as Alibaba and Tencent to circumvent PRC restrictions on foreign investment by setting up a structure of complex contracts between the mainland entity and a series of offshore shells. Under Chinese law, they are not recognised. Yet for years they have operated in plain sight of regulators as the structure which enables these firms to list in markets such as New York. Comfort levels received a boost in December 2021 when China published draft rules requiring companies, including VIEs, to file with the CSRC when applying for a listing on a non-China exchange. This was followed by a 'negative list' of businesses in which foreign investment is prohibited requiring approval from PRC regulators: if your business is on the list, an overseas IPO must meet a steeper hurdle. The very fact that VIEs had received a mention was taken as a tacit tolerance.

A political storm over inspection of mainland audit firms has concluded

All is fair in inspections and politics?

A decades-long tug of war between Washington and Beijing over inspection of China and Hong Kong audit firms with US listed companies as clients finally came to a close in August 2022. That month, the China Securities Regulatory Commission (CSRC) and Ministry of Finance (MOF) agreed to give the US Public Company Accounting Oversight Board (PCAOB) the ability to select firms and audit engagements to inspect, view complete audit working papers and interview audit personnel. The PCAOB swiftly got to work. Over nine weeks between September and November 2022 they sent more than 30 staff to conduct on-site investigations in Hong Kong.

Hong Kong and PRC audit firms have been sanctioned by the US

Fast forward to November 2023 and the PCAOB announced its first major enforcement settlements with PRC and Hong Kong firms since securing "historic access" to inspect firms under the deal with Chinese regulators. The details were released with much fanfare, including a fact sheet on the "historic sanctions" and a strong-worded press release by the PCAOB. "The days of China-based firms evading accountability are over," said PCAOB Chair Erica Y. Williams. "The PCAOB will take action to protect investors on US markets and impose tough sanctions against anyone who violates PCAOB rules and standards, no matter where they are located."

PWC was fined after staff shared answers on internal training tests

The violations in question? Failing to detect or prevent staff at PWC Hong Kong and China from sharing answers on internal training tests resulted in a total fine of US$7 million imposed by the PCAOB. Mainland firm Shandong Haoxin meanwhile attracted US$940,000 in penalties from the PCAOB for falsifying an audit report, failing to maintain independence from an issuer client and improperly adopting the work of another accounting firm as their own.

China edges up to 5th place with a higher score of 69%

2.2 Enforcement

This is China's best performing sub-category in our scoring where it boosted its score from 64% in 2020 to 69% in 2023, moving up a place to rank 5th. We observed stronger enforcement outcomes since the amended Securities Law took effect in March 2020, especially in the areas of delisting and false disclosure. Moreover, we marked up the score for the CSRC's willingness to work with the US Public Company Accounting Oversight Board (PCAOB).

Delisting reform has an impact

An unprecedent wave of delistings

The effect of changes in the delisting rules had a marked effect in taking "zombie" companies off China's stock markets. The changes date back to November 2020 when the Commission for Deepening Overall Reform, a policy body under the Party's Central Committee, approved the"Implementation Plan for Improving the Delisting Mechanism for Listed Companies". The two exchanges wasted little time in revising the listing rules the following month. Notably, the 2020 listing rules tightened the requirements for four types of mandatory delistings ie, those triggered by certain trading situations, poor financial conditions, disclosure and compliance deficiencies, and material violations of law. Some notable changes to the delisting criteria:

- **Trading situations:** a company's share price closes below RMB1 for 20 consecutive trading days (colloquially known as "one-yuan delisting"); a company's market value falls below RMB300m for 20 trading days in a row.

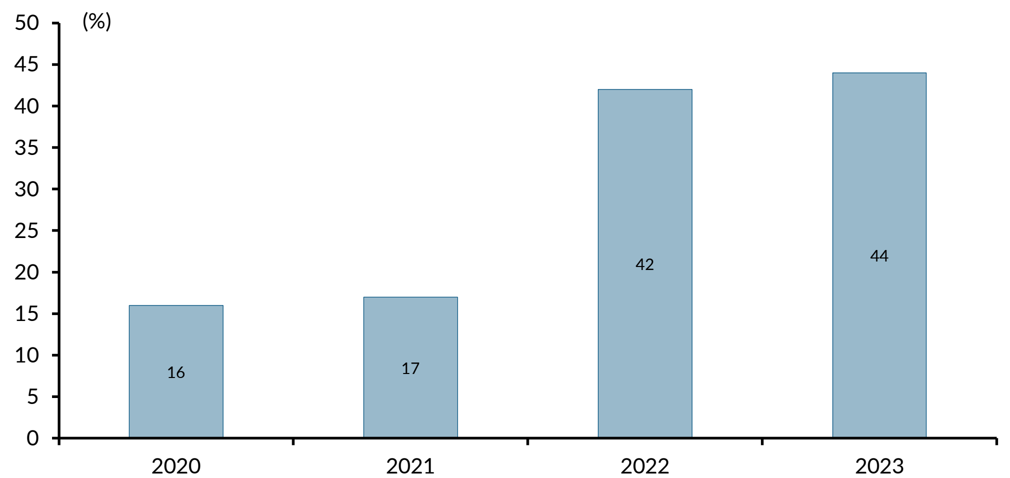
- **Poor financial conditions:** a company's operating revenue is less than RMB100m coupled with a net loss. A noteworthy amendment here was to take revenue generated from non-core business out of the equation.
- **Disclosure and compliance deficiencies:** major deficiencies in information disclosure; more than half of board directors fail to ensure the accuracy of semi-annual and annual reports and don't take any remedial measures.
- **Material violations of law:** new quantitative indicators for financial frauds were introduced.

Strong enforcement leads to a record number of delistings

Regulators have taken a tough enforcement stance, as encapsulated in the CSRC's slogan "companies which should be delisted must all be removed" (yingtui jintui) As a result, a total of 103 companies were mandatorily delisted between 2021 and 2023. To put this number in context, there were 64 mandatory delistings from 1999 to 2019, according to the Wind database. Notably, the number of delistings more than doubled from 17 in 2021 to 42 in 2022. The figure hit a record high of 44 in 2023.

Figure 6

Mandatory delistings on the rise, 2020-2023



Source: China Business Network

A breakdown of mandatory delistings

An overwhelming majority of these delistings were trigged by abysmal financial performance and exceptional trading situations. There was a bump in "one-yuan delisting" cases in 2023, with 20 cases compared to one in 2022. The number of delistings triggered by major violations of law also increased from one in 2022 and four in 2023.

Highlights of other enforcement efforts in 2021:

371 enforcement decisions in 2021, including eight blockbuster fines

- The CSRC issued 371 enforcement decisions, up 6.3% from the previous year. Total fines and confiscated gains amounted to RMB4.55 billion (US$619m). A total of 95 individuals were banned from entering the market.
- The regulator meted out eight RMB100m-plus "blockbuster" fines. Among them included a total fine of RMB482m (US$66m) levied on streaming video service Le.com and its co-founder Jia Yueting for false and inadequate financial disclosures from 2007 to 2016. In a smaller case, Guangdong Zhengzhong Pearl River Accounting Firm, the longtime auditor of Kangmei Pharmaceutical, received a RMB57.3m (US$7.8m) fine for its failings.

- Of the types of misconduct, 110 cases were related to inside trading, 106 to false disclosure, 21 to market manipulation.

Highlights for 2022:

Tough enforcement action continued in 2022

- The number of administrative penalties imposed by the CSRC rose slightly to 384, but fines and confiscated gains dropped to RMB2.67 billion (US$368m), a 40% decrease from 2021. 70 individuals were banned from securities trading.
- There was no shortage of egregious cases, despite fewer blockbuster fines. Notably, a retail investor in Fujian was given a RMB428m (US$59m) penalty for manipulating prices of eight stocks through a total of 145 brokerage accounts. In a first since the 2020 Securities Law, Shanghai Yingyi Investment Center, a shareholder of Wuxi AppTec, was fined RMB200m (US$28m) for selling about 17 million shares without proper disclosure.
- 135 enforcement decisions were related to disclosure violations, 79 to insider trading, and 11 market manipulation. It is worth highlighting that the number of false disclosure cases surpassed that of insider trading ones.

Highlights for 2023:

Significant increases in enforcement decisions and fines in 2023

- The CSRC handed out 539 administrative penalties, a 40% jump from the previous year. Fines and confiscated gains also more than doubled to RMB6.39 billion (US$880m). Meanwhile, 103 individuals were banned from entering the market.
- The regulator issued seven RMB100m-plus fines against market manipulators, including senior executives of listed companies, hedge fund managers and big retail investors.
- Overall, false disclosure and insider trading still featured heavily in the enforcement activities, with 189 and 84 cases respectively.

Figure 7

Key CSRC enforcement facts, 2021-2023

Year	Number of enforcement decisions	Total fines and confiscated gains (Rmbbn)	Number of individuals banned from market
2021	371	4.55	95
2022	384	2.67	70
2023	539	6.39	103

Source: CSRC, ACGA analysis

3. CG rules

China's score remains unchanged at 63%, but its ranking falls to 9th

China's score in this category stayed the same at 63%, but its ranking fell from 7th to 9th as other markets such as India, Korea and Taiwan have been fine-tuning their CG rules. Scores did not change in 20 out of 24 questions. One notable area where China lost points was its CG code, which has not been updated since 2018. A bright spot was the revamped rules on independent directors as a result of the 2023 reform. Other areas where China gained points included CG reporting rules and the prohibition of insider trading.

China's strong and weak areas in CG rules

China earned high scores in five questions related to disclosures of substantial ownership, directors' on-market share transactions, share pledging, price-sensitive information and voting results. It continued to receive low scores however in questions about blackout periods for director trading, nomination committees and ESG reporting standards.

The State Council sets the tone in INED reform while the CSRC develops rules

Reforming the independent director regime

In April 2023, the State Council kicked off reform of the independent director system, which was introduced in 2001, by issuing the "Opinions on the Reform of the Independent Director System of Listed Companies". This high-level circular sets out tasks in eight areas ranging from selection, nomination to the process of discharging duties. Based on the Opinions, the CSRC in August 2023 issued the "Measures for the Administration of Independent Directors of Listed Companies", which replaced the 2022 rules on INEDs.

A tighter definition of independent director

A notable feature of the Measures is the tighter definition of independent director, which mandates an INED to be free of any "direct or indirect interest" with the issuer and its majority shareholders. Article 6 addresses the issue of independence, listing six types of unsuitable INED candidates. Newly added to the list are those who have "major business dealings" with controlling shareholders and actual owners of the company. Article 7 complements this by specifying qualifications and skills for independent directors. Notably, an INED shall have at least five years' experience in law, economics, and accounting (the newly added skill).

INEDs have a greater say in auditors and conflict-of-interest management

Another key point of the Measures is to give INEDs more supervisory powers, particularly regarding the appointment of external auditors and the management of potential conflicts of interest. The 2022 rules require the approval of all independent directors to engage an external auditor or consultancy. The Measures lower the approval threshold to half of all INEDs. Additionally, INED approval is required for matters with significant conflict-of-interest risk, including related party transactions subject to disclosure and proposals made by an issuer and its related parties to change or waive undertakings. Such matters shall be deliberated at meetings attended only by INEDs.

Positive changes to concurrent directorships, nomination, and pipeline

Other significant changes include:

- **Concurrent directorships**: The maximum number of concurrent directorships in "domestic listed companies" is reduced from five to three (Article 8).
- **Nomination**: Investor protection organisations can entrust shareholders to nominate INEDs (Article 9).
- **Pipeline**: The China Association for Public Companies (CAPCO), a quasi-regulatory entity under the CSRC, will be responsible for building a database of INEDs (Article 16).

Improvements in CG reporting, pre-emption rights and insider registration system

Other rule improvements

Besides the new rules on independent directors, improvements have also been made in the following areas:

- **Disclosure of "major events":** In March 2021, the CSRC amended a key policy document on corporate disclosure, the "Administrative Measures for the Disclosure of Information of Listed Companies", for the first time since 2007. Notably, Article 22 tightens the disclosure of "major events" that may have a substantial impact on share prices. The expanded list of "major events" covers share buybacks, restructuring, major changes to accounting policies and criminal penalties given to directors, among others. It is worth noting that Article 12 removes the requirement for quarterly reporting. This is in line with the Securities Law, which mandates listed companies to publish annual and interim reports. The CSRC gives stock exchanges the leeway to require quarterly reporting. The Beijing, Shanghai, and Shenzhen stock exchanges still maintain this requirement.

- **Disclosure of board meetings:** In June 2021, the CSRC revised the content requirements for annual reports (ie, "Standards on Contents and Formats of Information Disclosure by Listed Companies No.2"). We are pleased to note that the disclosure requirements for board meetings have been strengthened. Article 32 requires issuers to divulge how directors perform their duties at the meetings, including any voices of dissent. Article 33 mandates the disclosure of the content of meetings held by board committees.

- **Pre-emption rights:** In February 2023, the CSRC imposed specific limits on non pre-emptive issuances in the revised "Administration of Registration of Securities Issuance by Listed Companies". Under the new rules, companies can issue shares to "specified" investors with the approval of two-thirds of shareholders at the AGMs. The issuance size is limited to RMB30m and less than 20% of net assets as of the end of the preceding year. Meanwhile, the issue price shall not go below 80% of the average share prices of the last 20 trading days prior to the reference date (ie, the first day of the issue period).

- **Registration system of insiders:** In January 2022, the CSRC fine-tuned the rules on the registration system of insiders (ie, "Regulatory Guidelines for Listed Companies No.5 - the System for Registration and Management of Insiders at Listed Companies"). The system, which was introduced in 2011, demands that listed companies create and maintain a file for each insider. The revised guidelines require the CEO and Board Secretary to confirm in written form the accuracy and completeness of these files. Moreover, stock exchanges are given the power to set disclosure requirements for the files.

Where China still does poorly

There remain limitations in China's CG rulebook. For example:

Weaknesses persist in stewardship code, NC, blackout periods and director nomination

- **Stewardship code**: The absence of a stewardship code remains a sore point. The Insurance Asset Management Association of China (IAMAC) is still working on a draft code for insurance asset managers.

- **Nomination committees:** There is no mandatory requirement for establishing nomination committees. As part of the independent director reform, the CSRC encouraged listed companies to set up nomination and remuneration committees composed mainly of INEDs.

- **Blackout periods for director trading:** In May 2022, the CSRC amended the rules governing director trading. But the blackout periods for directors and key management remain intact: 30 days before the release of annual results and 10 days before the announcement of interim results.

- **The ability of minority shareholders to nominate directors:** The ease with which minority shareholders can nominate directors is not clearly defined. Article 115 of the Company Law, effective from 1 July 2024, allows shareholders with a minimum 1% stake to put forward a resolution at the AGM, without specifying the types of resolutions. However, these shareholders can nominate independent directors under the "Measures for the Administration of Independent Directors of Listed Companies".

- **Dual class shares:** The Company Law (Article 144) allows unlisted companies to issue "shares with special voting rights", while listed companies are prohibited from doing so. According to the latest listing rules, companies with a dual-class stock structure can be listed on the Shanghai, Shenzhen, and Beijing stock exchanges if they meet requirements for expected market capitalisation,

revenue, and net profit. Such a structure must be approved at a shareholders' meeting with a two-thirds majority prior to listing (the listing rules of the Beijing Stock Exchange do not mention this requirement).

The Company Law also identifies certain matters that "may affect" the rights of dual-class shareholders, including amendments to the articles of association, changes in registered capital, mergers, split-ups, dissolution, and changes in company form (Article 146 and 116). These changes require the approval of a two-thirds majority at a separate class meeting of dual-class shareholders and a general meeting of all shareholders. In contrast, the rights of minority shareholders are addressed in only two places: 1) companies issuing dual-class shares must include provisions on investor protection and restrictions on transferring these shares in their articles of association (Article 145); and 2) holders of dual-class shares have the same voting rights as ordinary shares when electing supervisors and members of audit committees (Article 144).

New climate reporting rules

ESG reporting guidelines finally arrive, with a local twist

China made headway on 8 February 2024 with the release of draft guidelines on ESG reporting for listed companies along similar lines to TCFD, but with a local twist. Social factors, particularly rural revitalization, and common prosperity, feature heavily in the rules.

A TCFD structure is adopted

The guidelines follow a TCFD structure, categorised into four key areas: Governance, Strategy, Targets and Metrics, and Risk Management. Issuers are only briefly encouraged to conduct scenario analysis and disclose Scope 3 data if they can do so. Nor are they required to disclose how they would incorporate ESG performance metrics into remuneration policies.

National development themes permeate social disclosure requirements

Some of the guidelines have a distinct political or domestic flavour, in particular the emphasis on social issues in line with the national development agenda. An entire chapter is dedicated to disclosure on "social information," which stresses rural revitalization and social contribution. Companies are strongly encouraged to support rural revitalisation efforts and disclose how they have integrated these initiatives into their corporate strategy, as well as detail their systems for implementing them. Issuers are also asked to disclose any charity and volunteering activities, along with details of the funds invested and human capital leveraged to achieve results. How this impacts a company's brand and business development should also be disclosed. This resonates with China's Common Prosperity initiative and ongoing rural revitalisation efforts.

4. Listed companies

China dropped to 11th place with a lower score of 39%

This was the only category where China lost points, dropping from 51% in 2020 to 39% in 2023 and slipping from 10th to 11th place, just ahead of Indonesia (36%). It is worth noting that seven out of the 15 questions had the highest score capped at 3 out of 5 or below. The low scores were due to changes in our evaluation methodology as well as long-standing areas of weakness. Chinese issuers performed poorly in areas such as the quality of ESG reporting, board diversity, board evaluations, director training, independent chairs, and the disclosure of executive remuneration policies. On a positive note, they scored well on questions related to independent director pay and the independence of audit and nomination committees. Additionally, board remuneration was disclosed on a named basis despite the lack of transparency in executive remuneration policies.

One issuer provides insight into the role of the Party Committee

An additional question we examined for China was how the 15 large caps disclosed information on the Party Committee. Only one state-owned issuer briefly highlighted the role of the Party Committee in its governance structure. According to the one-paragraph disclosure, the shareholders' meeting serves as the "corporate organ of power", while the Party Committee "oversees the overall direction" and "facilitates implementation". The board is responsible for setting strategies and managing risks, while the management team focusses on the business operations and executes strategy.

Where China does well or above average

The best-performing areas are those with mandatory requirements

As with many other markets, Chinese issuers perform well in areas where regulators set mandatory disclosure requirements. Since 2003, the CSRC has issued a set of disclosure rules for listed companies titled "Standards on Contents and Formats of Information Disclosure by Listed Companies". Among them is Document No.2, last amended in June 2021, which sets out the disclosure requirements for annual reports.

Disclosure of directors' remuneration has gaps

Notably, Document No. 2 (Article 31) requires issuers to disclose the pre-tax remuneration paid to each director, supervisor, and senior executive by "the company". All of the 15 large caps complied with this requirement, achieving an average score of 4. However, 13 out of the 15 did not report the remuneration of non-executive directors who were from parent companies or major shareholders, and therefore not paid by the issuer. At one state-owned utility company, nearly half of the board (six out of 13) fit this category, and their remuneration was not disclosed.

Independent director pay is a bright spot

The disclosure of remuneration for independent directors was clear. All issuers scored a perfect 5, with independent directors receiving fixed fees without excessive benefits or bonuses found in some other markets.

Where China does averagely

Compliance mentality guides board governance reporting

The quality of board governance reporting is on par with the regional average. One notable trend in scoring this question is the narrow disparities between scores: ten out of the 15 received a score of 2, while the rest achieved higher scores ranging from 2.5 to 3.5. All issuers adhered to the CSRC's requirements by disclosing the date of each board meeting and the matters approved by the board. But none of them provided further insight into the topics discussed. The tick-the-box mindset was also evident in the disclosure of directors' biographies. Issuers often provided basic information about director's experience but fell short of explaining the reasons for their nominations.

Figure 8

China listed companies scores, CG Watch 2023

Question	Average score	Range of scores
1. Does the company's board governance reporting compare favourably against international best practice?	2.3	2-3.5
2. How would you rate the quality of the company's ESG/sustainability reporting?	0.8	0-2
3. Does the company provide comprehensive, timely and quick access to information for investors?	1.8	0-2
4. Does the company undertake annual board evaluations, either internally or using external consultants?	0.1	0-1
5. Does the company disclose and implement a credible board diversity policy?	0.5	0-3
6. Does the company provide induction and/or ongoing training to all directors?	0.8	0-3
7. Does the company have an independent chairman and/or a lead or senior independent director?	0	All get 0
8. Does the company disclose total remuneration of each member of the board of directors?	3.7	3-5
9. Are the independent directors paid partly or wholly in stock options or restricted share awards? Do they share in a percentage of company earnings or other commissions in addition to their base fee?	5	All get 5
10. Are audit committees (or an equivalent) independently led and competent in financial reporting/accounting matters?	3.5	2-5
11. Does the company have an internal audit department that reports to the audit committee?	3	All get 3
12. Does the company provide a detailed explanation of its executive remuneration policies?	0.5	0-2
13. Does the company have a nomination committee and is it independently led?	3.2	2.5-4.5
14. Does the nomination committee have a female chair or at least one female director?	0.5	0-5

Source: ACGA research. Based on 15 large caps from a range of sectors

ACs are independent, but their competence varies

China scored well on the independence of audit committees (AC). All issuers had an independent director serve as the AC chair. However, there is a concern about the competency of ACs. Chinese companies commonly appoint professors to ACs, particularly those specialising in economics and management. We also found AC members with backgrounds in engineering, law, and medicine.

Limited disclosure on the operation of internal audit

On a related question, all issuers had an internal audit department under the AC. But only one steel maker provided limited information on how the internal audit interacts with the AC.

All NCs have an independent chair

Issuers also performed relatively well in terms of the independence of nomination committees (NC). In the 2023 rules on independent directors, the CSRC encouraged listed companies to set up nomination committees. It is refreshing to find that all of the 15 large caps had a NC led by an INED. The situation is less encouraging in terms of the frequency of NC meetings. Ten out of the 15 stated that their NCs met twice or more during the year, while the rest either held fewer than two meetings or did not disclose the meeting frequency.

Where China performs poorly

ESG reporting lags behind regional best practice

Chinese companies received low scores on the quality of ESG reporting, with 12 out of the 15 scoring 1 or below. Most issuers did not address material issues in detail, instead focussing on their social responsibilities such as community services, volunteering activities, and donations. Only one electronic components manufacturer provided a detailed assessment of materiality.

Women have yet to hold up half the sky

Scores were also low on the disclosure of board diversity policies. Two-thirds of the issuers had boilerplate and generic policies, resulting in a score of 0. Only one set a clear target for gender diversity on the board. This lack of commitment to board diversity led to low rates of female representation on boards. Only three issuers, all privately-owned, had at least 20% of women on their boards. The presence of other forms of diversity on boards was also rare, with only one company having a foreign director.

Limited female representation on NCs

Given the lack of gender diversity on boards, it is not surprising that only three out of the 15 large caps have at least one female director on their NCs. However, one privately-owned company stood out for having an all-female NC.

Weak board evaluation practices

Board evaluation is another area of weakness. Only two out of the 15 disclosed that their supervisory boards conducted board evaluations, without providing details on assessment methodologies and results. Most other issuers did not mention board evaluation, even though they require supervisors to "monitor" or "supervise" the performance of directors in their articles of association. There are concerns about the effectiveness and independence of the supervisory board as supervisors generally hold lower rank and standing than directors. It is worth noting that the 2024 Company Law allows companies to replace the supervisory board with an audit committee composed mostly of INEDs.

Lack of transparency in executive remuneration policies

The disclosure of executive remuneration policies was minimal. None of the 15 provided a clear explanation of the components of the remuneration and the parameters of KPIs. Three fared slightly better with a score of 2, while the rest scored only 0.5 or 0. Some examples of generic statements: the remuneration for executives is based on "the results of their work in ethics, competence, attendance and performance", or on "internal rules about remuneration management and performance evaluation". On a more positive note, three issuers considered "sustainability performance" when evaluating executive remuneration, and one disclosed a clawback policy.

Director training appears to be selective

The provision of director training seemed selective. Nine out of the 15 issuers claimed to offer training for directors but did not provide details about the topics, duration, and the names of the participants. Among these nine issuers, only two disclosed that the training covered all directors. While the quality of board director training has improved since the last CG Watch, there is still a long way to go in terms of disclosure.

No lead INED, but there is hope

None of the 15 had an independent chair or lead INED. As we mentioned in the CG rule section, issuers under the new independent director regime are required to hold meetings attended only by INEDs. To fulfil this requirement, an INED must be appointed to convene and lead the meetings. This INED serves a role similar to a lead INED. This development may improve the score on this question in future surveys.

None of the issuers provide named IR contacts

Lastly, Chinese issuers can instil more confidence in investors by providing detailed IR contact information. None of the 15 provided the names and contact details of their IR team. Additionally, we found that one company's website was inaccessible at the time of writing, using the link provided in its 2023 Annual Report.

ACGA research in 2023 found only 14% of directors at the top 100 to be female

The gender gap
ACGA in August 2023 conducted research into the top 100 in China to see how many women are being appointed to boards. We found only 14% of directors at China's top 100 companies are female. What is equally concerning is the absence of pressure for companies to do better.

There are no specific rules on gender diversity

Hong Kong and Korea have officially banned single-gendered boards, and Japan has taken substantial steps to promote diversity. In stark contrast, China has yet to introduce any specific rules or quotas from regulatory bodies to encourage gender diversity on corporate boards.

Civil society attempts to raise awareness

Civil society lags in this regard. The Xiangmihu Female Board Member Initiative, established in 2020 as an advocacy group for female board directors, initially gained support from the State-owned Assets Supervision and Administration Commission (SASAC), local asset managers, and companies. But the primary focus of the initiative is still only to raise awareness.

Female rights are still a significant issue

In China, gender discrimination in hiring practices and promotion evaluations remains a pervasive issue. A 2017 survey officially revealed that about 54% of women were questioned about their marital and childbearing status during job interviews. While some regulations have been introduced to provide stronger protections for women, such as the revision of women's protection to address workplace sexual harassment, China's declining birth rates have also shifted the focus toward women's roles in family life, emphasising the importance of respecting family values.

Foreign investors are putting more emphasis on gender diversity

Still foreign investors are placing emphasis on board diversity. Asset managers such as LGIM have been advocating diversity within their investee companies, expanding their diversity engagement to include emerging markets, including Brazil, India, and China. BNP Asset Management runs a global diversity campaign. Fidelity International sets a requirement of 30% female directors for developed markets and 15% for developing markets, while BlackRock® mandates at least one female director for large companies in mainland China.

5. Investors

China ranks 11th on a score of 22%

China's score in this category increased slightly from 18% in 2020 to 22% in 2023. It however continued to swim at the bottom, ranking 11th. There has been a renewed emphasis from regulators on investor involvement in corporate governance. But the asset management industry is still waiting for the advent of a stewardship code.

A wide disparity between leaders and laggards of stewardship

Scores improved on questions about voting by domestic institutional investors, engagement by foreign institutional investors, and the operation of local proxy voting advisors. Yet this can hardly hide a wide disparity between the leaders and laggards of stewardship in China. While leading domestic asset owners and managers have implemented responsible investment and have been increasingly active in voting, the picture is quite different at smaller funds.

Low retail participation in CG, but class actions are on the rise

The retail participation in corporate governance meanwhile is still low, despite sporadic rebellions. On a more promising note, we saw China's second securities class-action lawsuit in 2023 involving financial reporting fraud at Essence

Information Technology, which inflated profits by RMB187m (US$25.8m) and revenue by RMB342m (US$47.2m) from 2016 to 2019 to qualify for listing.

Waiting for a stewardship code

An old regulatory theme, more strongly emphasised

Regulators have shown a stronger intention to push forward investor stewardship, which is aligned with their bigger policy goals of improving the quality of listed companies and attracting more long-term investors to China's retail-dominated stock market. This is evident in the "Opinions on Accelerating the High-quality Development of the Mutual Fund Industry" issued by the CSRC in April 2022. Among the 16 strategic tasks outlined in the Opinions, there was one about "practicing social responsibility". Notably, institutional investors were encouraged to "actively participate in the governance of listed companies", "voting not only with feet but also with hands". Recall that the 2018 CG Code also encourages "reasonable" investor participation in corporate governance. While this regulatory theme is not revolutionary, the wording used in the 2022 Opinions is unequivocally stronger.

The CSRC plans a stewardship code

In July 2023, the CSRC further disclosed in a press interview that it would develop "behaviour guidelines" on investor involvement in corporate governance (ie, the stewardship code), without providing any timelines. Separately, as we mentioned earlier, the Insurance Asset Management Association of China (IAMAC) has been drafting stewardship guidance for the insurance sector.

A sharp difference between leading players and the rest

Leading players play a constructive role in promoting stewardship

All of the top five asset owners and top 10 asset managers in China have policies on CG or ESG. For example, the two biggest domestic asset owners, China Investment Corporation (CIC) and National Council for Social Security Fund (NCSSF), have incorporated responsible investment into their investment principles. NCSSF has also developed ESG-related indicators for assessing external managers who now manage two-thirds of its assets.

Domestic asset managers vote more while local proxy advisors continue to grow

Half of the top 10 domestic asset managers have a voting policy. According to an interview with local proxy advisor ZD Proxy Shareholder Services in early 2024, big domestic institutional investors have become more active in voting in recent years. Funds with an AUM of over RMB100 billion now attend an average of 10-22 AGMs per year. Moreover, they are more willing to voice discontent on matters with which they disagree, especially regarding RPTs, stock options, and financing. The expansion of ZD Proxy's company coverage (nearly 800 A-share issuers as of February 2024) indicates a greater demand for voting guidelines. Having said that, none of the top 10 asset managers surveyed disclosed their voting records.

Smaller institutional investors remain on the sidelines

It is worth emphasising that the vast majority of smaller institutional investors are still reticent to act as stewards of listed companies. A CG/ESG policy is hard to come by among medium and small-sized funds, and many of them still consider voting useless. Part of ZD Proxy's job has been educating asset managers on the importance of voting with their shares.

Corporates are urged to open doors for investors

A perennial hurdle on the engagement front is gaining corporate access. The situation however has been slowly improving. The "Guidelines for Managing Investor Relations at Listed Companies", amended by the CSRC in April 2022, require issuers to be more "proactive" in investor relations (Article 4). In early 2024, ACGA's China Working Group, after nearly four years of communication, secured a face-to-face meeting with Kweichow Moutai, China's biggest public company by market capitalisation at the time of writing. We hope this momentum continues.

Low retail participation in AGMs

Sporadic retail activism and rising class actions

Participation in AGMs by retailer shareholders in China remains notably low. About one in 20 (5.2%) shareholders surveyed by the China Securities Investor Services Center (CSISC), an affiliate of the CSRC, voted at AGMs in 2022, compared to 6.3% in 2021.

Sophisticated retail shareholders rebel against badly run companies

Rebellions and collective actions by retail shareholders were occasionally found at widely-held and underperforming companies. In a rare case in April 2022, Liaoning SG Automotive saw seven shareholders with a combined stake of 14% requisition an EGM to halt an acquisition and replace the entire board. In another case, a shareholder of Netac Technology put forward a resolution to dismiss the board chairman in November 2023.

The momentum on class actions continues

Another positive development in China's retail investor space has been the use of the special representation litigation mechanism, the Chinese-style securities class action regime, for investor compensation. The mechanism, introduced by the 2020 Securities Law, was first used in the landmark Kangmei case in 2021. In July 2023, the CSISC sued the software maker Essence Information Technology for financial reporting fraud on behalf of a group of investors, marking China's second special representative action. The lawsuit was settled through mediation in December 2023 when the Shanghai Financial Court ordered the company to pay RMB280m (US$38.8m) to nearly 7,200 investors.

6. Auditors & audit regulators

China's score increases to 49% but the market still ranks 12th

China's score in this category increased by six percentage points to 49% but its ranking remained at the bottom. China still maintains an unequivocally centralised audit regulatory regime, with the government setting the tone, themes and priorities. There is no independent audit regulator distinct from government. But the government has in recent years stepped up inspection, investigation and sanction, which boosted scores on two questions about audit oversight and disciplinary control. Scores remained unchanged on the other eight questions.

Barren soil for independent audit regulators in China

Centralised audit oversight

In China's audit regulatory system, the Ministry of Finance (MOF) functions as the overarching body to set accounting standards, supervise accounting firms and take disciplinary actions. The China Institute of Certified Public Accountants (CICPA), overseen by the MOF, shares some inspection duties, manages registration and training, and drafts auditing standards and the code of ethics. Additionally, the CSRC, elevated to be a government agency directly under the State Council in 2023, plays an increasingly active role in regulating accounting firms which engage in securities business (ie, those which provide annual audits of listed companies and auditing services for IPOs, M&A, and financing).

Regulatory urgency to discipline accounting misbehaviour

China still does not have an independent audit oversight board under such a regulatory framework. But one positive development is that the government has noticed the inadequacy of auditing firms in performing their "gatekeeping" duties and has taken a tougher enforcement stance. In July 2021, the State Council issued a landmark directive, titled "The Opinions on Further Standardizing the Financial Audit Order and Promoting the Sound Development of the Certified Public Accountant Industry" ("the 2021 directive"). While the directive touched on such mid- and long-term areas for improvement as quality control systems in accounting firms and accounting laws, the key prong was to tighten the supervision of accounting firms which engage in securities business. In China, accounting firms

must file records with the MOF and the CSRC to undertake securities business. CICPA's data shows that there were 115 accounting firms with a securities qualification as of April 2023.

The MOF hones in on large accounting firms

Based on the 2021 directive, the MOF promulgated the "Measures for the Supervision and Inspection of Accounting Firms" in April 2022, setting inspection frequencies and identifying key risk areas. Notably, the Measures zeroed in on big firms which audited SOEs and listed companies: firms with annual revenue exceeding RMB1 billion would be subject to annual inspections, while those with annual revenue between RMB500m and RMB1 billion would be visited once every three years. Provincial finance departments would conduct inspections, with special attention given to risk areas such as auditor independence, audit quality, and information security.

The CSRC and CICPA share inspection and enforcement duties

The CSRC is another key government agency that monitors and sanctions accounting firms in the securities domain. It dished out penalties to six accounting firms in 2020. The number more than doubled to 16 in 2022. Additionally, CICPA supplements the enforcement work with annual inspections of accounting firms in non-securities domains. Its recent inspection plans aimed to cover at least 20% of these firms across China. In 2022, it found irregularities at 259 out of 1,864 firms it inspected. As a result, 163 firms were summoned for a meeting.

The MOF is usually a black hole on disciplinary outcomes

There is still little disclosure on the government's inspection and disciplinary work. The only major accounting case published on the MOF's website since 2020 relates to Deloitte's audits with state-owned asset manager Huarong, in which the Ministry in March 2023 fined Deloitte's Beijing office RMB211.9m (US$30.8m) and suspended its operation for three months.

Disclosure of disciplinary work improves but remains limited

But the MOF did improve the disclosure of disciplinary actions taken against smaller firms. Its Supervision and Evaluation Bureau occasionally published administrative penalties levied against local firms and, in some cases, provided detailed accounts of auditing irregularities ranging from mistakes in recognising revenues to lapses in professional judgement.

Lack of English-language disclosure on enforcement

On a promising note, the CSRC regularly updates administrative penalty decisions on its website. CICPA also publishes inspection reports, albeit less frequently. It is worth noting that the enforcement disclosure is still only available in Chinese.

Promoting auditor independence around domestic themes

Regulators emphasise audit independence in the key policy text

China's audit regulators recognise auditor independence as an indispensable element of audit quality, especially for large SOEs and listed companies. Independence of auditors and accountants was mentioned three times in the 2021 directive.

The MOF fine-tunes rules on auditor selection and rotation

It was not until February 2023 that the MOF took a further step by issuing the "Measures for the Administration of Selection and Engagement of Accounting Firms by State-Owned Enterprises and Listed Companies". The Measures specified criteria for auditor selection and set auditor rotation requirements. More specifically, it required SOEs and listed companies to change partners of audit projects and the signing of CPAs every five years. Moreover, SOEs shall not "in principle" hire the same auditor for eight years, which is largely in line with the auditor rotation policies set out in a 2011 directive for Chinese central state-owned enterprises.

CSRC mulls over mandatory auditor rotation

The Measures, however, were silent on how long a listed company can have the same auditor. In February 2023, the CSRC said in response to proposals at the annual meetings of the National People's Congress that it would explore the feasibility of mandatory auditor rotation for listed companies.

The MOF strengthens code of ethics in line with domestic imperative

In terms of auditor ethics, there has been no significant development on the further adoption of the International Code of Ethics for Professional Accountants. Efforts on the ethics front have revolved around the theme of "integrity building" brought forward by President Xi Jinping. In January 2023, the MOF issued a Code of Professional Ethics for Accountants, outlining three guiding principles around integrity, continuous learning, and strict adherence to accounting standards. The principles were exceedingly concise compared to CICPA's Code of Ethics for CPAs, which was last amended in December 2020. But they carried symbolic and political importance. A nationwide learning campaign soon followed.

Standards convergence at China's own pace

China wants to have a say in shaping international standards

"The 14th Five-Year Plan Outline for Accounting Reform and Development" issued by the MOF in November 2021 offer glimpses into the government's approach to standards convergence. The baseline is to "dynamically" align China's own accounting and auditing standards with the international requirements. This process entails adapting international standards to the Chinese corporate realities. Moreover, the five-year plan underscored China's role in shaping the international standards. In practice, Chinese Accounting Standards (CAS) have been substantially converged with the IFRS, with discrepancies existing in areas such as valuation of fixed assets, the impairment of loss on an asset and classification of accounts. Although China is committed to having some domestic companies adopt IFRS, there is no timeline for this goal.

Adoption of IFRS 17 is still in its early days

One noticeable development in China's standards convergence progress is the implementation of China's equivalent of IFRS 17 on the accounting of insurance contracts. China's version of IFRS 17, "The Accounting Standards for Business Enterprises No. 25 - Insurance Contract", was unveiled by the MOF in December 2020. Dual-listed insurance companies were mandated to adopt the new standards by January 2023 while other insurers were required to do so by the beginning of 2026. In 2023, Ping An Insurance became one of the first insurers to apply IFRS 17 to the disclosure of financial results. Other insurance giants followed suit, including China Pacific Insurance, the People's Insurance, and China Taiping Insurance.

CICPA amends auditing standards for better alignment

China's auditing standards meanwhile are closely aligned with the International Standards on Auditing. In 2022, CICPA made wide-ranging amendments to Auditing Standards for CPAs in China, covering areas such as risks of material misstatement (No. 1211) and the audit of accounting estimates (No. 1321).

7. Civil society & media

China ranks 12th with a higher score of 26%

China's score improved by four percentage points to 26% in this category, but it still ranked last, well behind the Philippines (33%) which ranked 11th. It gained points on two questions: the quality of director training and the efforts made by NGOs to raise CG standards. But it lost ground on one question about whether professional organisations work to raise awareness of good corporate governance. Scores remained low on the other six questions we ask, which dented the market's overall performance in this category.

The quality of director training improves

Four main providers of director training

Four main organisations in China regularly provide training for directors, board secretaries, supervisors, and senior executives of listed companies: the China Association for Public Companies (CAPCO) as well as the Shanghai, Shenzhen, and Beijing stock exchanges. A lesser-known organisation that undertakes board secretary training is the China Capital Market Institute, set up by the CSRC and the Shenzhen Municipal Government in 2012.

The breadth and depth of training improve

CAPCO and the Shanghai and Shenzhen exchanges all have well-established online learning platforms, while the Beijing exchange's e-learning platform was still under maintenance as of early June 2024. The CAPCO's platform, for example, features video courses on a wide range of topics from regulatory policies, CG basics, and investor relations to shareholder rights, financial statement analysis, and ESG reporting. In addition to online training, all four offer multi-day, offline courses for directors, supervisors and board secretaires.

More INEDs participate in training, spurred by reform

One positive development in the director training space is that more INEDs have participated in training. The Shenzhen stock exchange discloses training records of new and existing INEDs on a named basis. In 2020, 1,350 INEDs received training from the exchange. The number almost tripled to 3,739 in 2023. As for the Shanghai stock exchange, 1,411 INEDs at mainboard-listed companies completed continuing training in 2022. The figure also jumped to 2,310 in 2023. One notable factor driving this trend was the reform of the independent director system. Notably, in August 2023, the CSRC required INEDs to "strengthen their continuous learning of securities law and regulations" (Article 34 of the "Measures for the Administration of Independent Directors of Listed Companies").

Sparks of NGOs

A Shenzhen-based NGO advocates for board diversity

One persistent area of weakness in China's CG ecosystem is the lack of NGOs dedicated to raising CG standards. As one of the few such NGOs, the Shenzhen Research Association of Corporate Governance deserves a mention for its efforts in promoting gender diversity on boards. In November 2020, it worked with the Shenzhen Public Companies Association and a small group of listed companies and institutional investors to launch the Xiangmihu Female Board Member Initiative, an advocacy group aimed at boosting female representation on boards. It is worth noting that the initiative also received support from the Shenzhen stock exchange and local financial authorities.

China SIF focusses more on the E and S of ESG

Another visible player in the ESG space is the China Sustainable Investment Forum (China SIF). It was launched by ESG consultancy SynTao Green Finance in 2012 and later registered as an NGO in Shenzhen. The forum organises conferences and publishes original research on responsible investment and sustainable finance in China, with a focus on environmental and sustainability issues.

Industry bodies touch lightly on CG

CG takes a back seat at industry bodies

Key professional organisations in China do not seem to prioritize CG issues. For example, CICPA regularly provides training for partners at accounting firms, covering topics such as Xi Jinping's economic theories, China's macroeconomy, digital transformation of accounting firms, and leadership skills. Conspicuously absent from the training agenda were CG-related topics. In another example, the Asset Management Association of China (AMAC) held two sharing sessions called "Sustainable Investment Mastermind Talks" in 2022 and 2023, both of which focussed on carbon neutrality and investment.

Key original research focusses on companies

Two major CG research centres in China

Two prominent academic institutions in China that focus on corporate governance are the China Academy of Corporate Governance at Nankai University and the Research Center of Corporate Governance and Enterprise Development at Beijing Normal University. The former conducts an annual survey on the quality of corporate governance at listed companies in China, using a quantitative evaluation system that covers six CG aspects (for example shareholders, board of directors, information disclosure). The latter also takes a company-based approach, producing a series of ranking tables on sub-areas of CG and ESG including financial management, shareholder rights, and voluntary disclosure.

Law firms decipher CG policies, while a legal journal introduces international CG experience

Law firms such as Grandall Law Firm, DeHeng Law Offices, and King & Wood Mallesons play an active role in analysing CG policy changes. Additionally, the Securities Law Review (Zhenquan fayuan), a quarterly journal run by the Shanghai Stock Exchange, publishes articles on CG topics, including insider trading, dual-class shares, proxy voting, and class actions. Notably, its editorial perspective is international, covering CG practices in China, the US, and Japan.

Chinese media "sing the main melody"

Chinese media are mandated to convey "positive energy"

Private capital has been barred from investing in news organisations in China since 2005. The 2022 Negative List for Market Access, issued by the National Development and Reform Commission and the Ministry of Commerce, reiterated this ban, prohibiting "non-public capital" from gathering news and distributing news produced by foreign media (Item 6 on the list). Given that all news media in China are state-owned, they must operate according to the principles and priorities set by the Party.

Media toe the Party line when covering CG

Under this media regulatory regime, Chinese media outlets strictly adhere to the official line when reporting on CG developments. They often provide lucid coverage of major CG policies but avoid delving deeper into the problems these policies seek to address. For example, the People's Daily on 29 August 2023 published a lengthy report on the overhaul of the independent director system, referring to rubber-stamp INEDs as "flower vase directors". No other media outlets explored the phenomenon of "flower vase directors" in greater detail.

Coverage on shareholder rights is the bright spot

On a more positive note, the issue of shareholder rights remains under the media spotlight. Leading financial outlets such as Caixin and the Securities Times run interesting stories of minority shareholders rebelling against troubled issuers, reminding the investing public of what is possible. Additionally, there is a monthly magazine, Director & Boards, dedicated to CG issues.

Downgrade watchlist

What to avoid

Factors that could force China's score to fall in 2025:

- ❑ A further blurring of practical lines between state and private enterprise
- ❑ Any loss of momentum in the nascent class action mechanism
- ❑ Diminished funds and resources which would enable regulators to take action against market miscreants
- ❑ A lack of improvement in the ability of investors to engage with corporates and access senior management and board executives
- ❑ Expansion of the dual class regime

Next Steps

Our recommendations for the next stage of CG reform in China include the following:

Granularity on the role of Party Committees

1. **Greater transparency on the role of Party Committees**: given the fortification of Party Committees in recent changes to the Company Law, investors would welcome enhanced visibility on how these committees interact with the board and how they influence the decision-making process on a micro basis.

Details of how the stock exchanges are funded

2. **Stock exchange disclosure**: it would be of great value for market analysis if the main stock exchanges could divulge their funding mechanism, annual budgets and capacity.

More insight into the work of boards would be welcome

3. **CG disclosure requirements**: greater visibility on the work of boards would provide investors with enhanced insight into the decision-making process, evaluations of directors, any skills gaps and remuneration. Stock exchanges could also encourage issuers to provide more tangible details in their CG disclosures. The 2018 CG Code is getting long in the tooth - an update would be welcome.

Investors could be better stewards

4. **Stewardship**: regulators or leading asset owners could take a more explicit leadership role in promoting stewardship. Improving their disclosure on stewardship policies and activities would help set the tone.

Better transparency on the work of audit regulation

5. **Audit regulation**: it is difficult even for a native Chinese reader to find information on how regulators set accounting and auditing standards and align them with global accounting language. Improved transparency in this respect would be beneficial, as would greater disclosure on enforcement work. The CSRC should also require listed companies to disclose non-audit work and fees: there is still no regulatory requirement to do so.

Company checklist

Actions companies could take to enhance CG practice and disclosure immediately

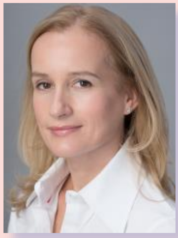
Actions companies could take over the short to medium term to enhance their governance practices and disclosure include the following:

1. **Board reporting**: close the remuneration reporting gaps. Full remuneration of each director should be disclosed, as well as the pay of non-executive directors, even if these individuals are nominated by controlling shareholders and hold positions within the appointing entity.

2. **Party Committees**: details of board interactions, the decision-making process and how these committees generally work in practice should be disclosed in unambiguous terms.

3. **Board leadership**: appoint an independent chair or lead independent director.

4. **Board diversity**: details of steps being taken to appoint more female directors would be welcome. It may not be on the regulatory agenda, but it is on those of foreign investors.



Jane Moir
Head of Research, ACGA
jane@acga-asia.org
+852 2160 1797

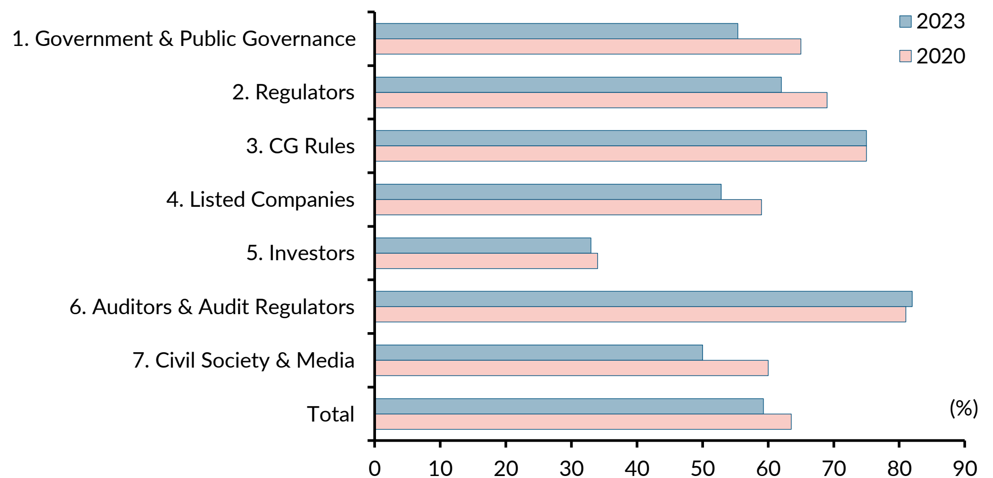
Hong Kong - Walking a tightrope

- The market tumbles 4.2 percentage points to joint sixth place in our rankings from equal second in 2020 with a score of 59.3%. A 10 percentage point drop in both the Government & Public Governance and Civil Society categories unseats Hong Kong as one of the historical top three CG performers in the region
- A changed political environment has impacted the role played by key institutions and stakeholders in the city's ecosystem, which in the past compensated for a lack of overall CG policy
- Recent market reforms have focussed on quantity of IPOs, with core guardrails lowered to entice listings and no counterbalancing initiatives, such as class actions, to level the playing field for investors
- A few upgrades to CG rules and regulations, and sustainability reporting begins to move forward (with a few bumps) along ISSB lines
- Hong Kong retains the top slot for enforcement as the SFC remains a robust enforcer and HKEX scolds more errant directors, but cross-border realities see absconders evade recourse and the market misconduct tribunal fails to bite
- Listed companies rank higher than their regional peers but on a lower score as overseas issuers with disclosure waivers drag down overall quality
- Domestic investors keep their heads down and stewardship stays largely under the radar, with policymakers not taking the lead here in recent years
- The auditing oversight body finds its feet and gets tougher with inspections and quality control
- Civil society, academics and media appear chastened amid fears of crossing red lines

Click to rate this research

Figure 9

Hong Kong CG macro category scores: 2023 vs 2020



Source: ACGA

Introduction

Hong Kong falls four places to rank 6th on a score of 59.3%

To quote Albert Einstein, nothing happens until something moves. There have been significant political and economic changes in Hong Kong since our last CG Watch in 2020 and given the wide range of factors we take into account in our scoring, there has been a notable fall in rank from second to sixth place. The once-predictable CG performer has shed 4.2 percentage points to score 59.3%, sharing its current position in the overall rankings with India. The categories where it saw the biggest drops in score were government & public governance and civil society & media, where Hong Kong lost 10 percentage points respectively. This reflects uncertainty surrounding the once-solid roles played by key cogs in the CG ecosystem, such as the judiciary, legislature and media. Elsewhere, although the market remains strong on enforcement it lost points in the regulators category, largely due to reforms since 2020 to widen the depth and breadth of listings which in our view has come at the expense of CG standards.

Gaps are emerging in disclosure depending on the type of issuer

One example of the impact of these market developments can be seen in the quality and breadth of disclosure listed companies are making. This was seen in remuneration disclosure, where details of executive pay at state-owned issuers and weighted voting rights (WVR) companies remain blank or partial, in contrast to Hong Kong incorporated companies. Overseas issuers, which account for a large share of the overall market capitalisation, receive myriad waivers on core CG requirements, from connected transactions to the takeovers code. This is creating an uneven playing field for listed companies in Hong Kong.

There was some progress with audit regulation

Progress can be seen in the oversight of auditors, as the regulator flexed its new powers and the CG rules category remained steady: the nuts and bolts of best practice is traditionally an area where Hong Kong puts in a respectable showing. It is a similar story with investors: although a point was lost, the foreign contingent do vote, and tell us how they vote, and engage with issuers. Less visible is what their domestic peers are doing on this front, just as retail investors seem a more frail contingent as a force for change.

A lack of CG direction in years past comes at a cost

ACGA has been in Hong Kong since 1999 and many of the points we have made in CG Watch of years past unfortunately remain relevant today: a corporate sector reluctant to embrace higher governance standards, and policy-makers who do not want to force them to do so. We made the point in our last CG Watch, when Hong Kong ranked 2nd, that a sophisticated financial centre should not be trailing Australia by such a wide margin.

Recapping CG Watch 2020

Easy CG wins are still up for grabs

There is not much to report in terms of progress on the recommendations we made in our last CG Watch and indeed the ones we recap in Figure 10 could still be easy wins today:

Our recommendations from CGW 2020

Figure 10

Hong Kong: recap of 2020

	Recommendations	Outcomes
1.	Adopt a universal whistleblowing law	No change
2.	HKEX to provide details of its regulatory budget and investment in technology	HKEX has provided more information on its technology investment
3.	Update the Stewardship Code	No change
4.	Develop a minority shareholder association to benefit retail investors	No change
5.	Lead independent directors as a CG Code provision	In June 2024 HKEX began a consultation on the possibility

Source: ACGA

1. Government & public governance

Hong Kong falls two places to rank 5th on a much lower score of 55%

This was one of Hong Kong's worst-performing categories, with the market slipping two places to rank 5th on a score of 55%, ten percentage points lower than 2020. It was narrowly beaten by Singapore, which also saw its score drop by a lesser four percentage points to 56%.

The lack of a clear CG policy and recourse for investors is a consistent theme

Hong Kong lacks an overarching CG policy. The government takes the lead on capital market reform via HKEX and in recent years this has been very focussed on IPOs (see also our section on Regulators), while the lack of recourse that exists for investors in the market remains the same. CG policy gaps over the years were somewhat compensated for by the institutions buttressing the financial landscape, such as an independent judiciary, outspoken legislature and robust securities regulator which can operate without political interference, either overt or implicit. Today, these institutions appear less forceful in supporting CG development.

A familiar story on policy

Listed company quality is not topping the policy agenda

Policymakers have made piecemeal CG reform over the years, making some improvements to market quality yet often submitting to a 'consensus' view that the time is not right, Hong Kong companies are not ready, or it is too burdensome for fledgling issuers. Family businesses and concentrated ownership have consistently stood in the way of cohesive CG development. In the recent past as Hong Kong rode an IPO boom, the welcome mat was laid out for more PRC 'homecoming' listings, WVR and SPACs. As the market took a turn for the worse, policymakers lowered entry requirements for overseas issuers, adopting a regime for 'specialist technology' stocks and setting up a special task force to seek a solution to its stock market's liquidity problem. Conspicuously absent from this government-led review is a long, hard look at the quality of listed companies. It was the now-CEO of the SFC, Julia Leung who in 2019 noted in a speech that a "consistent theme" to emerge from research and stakeholder engagement was that the lack of turnover and liquidity in a "certain segment of our stock market" related to perceived problems with listed companies and securities. Our Listed Companies section paints a disappointing picture of disclosure that investors can expect in Hong Kong.

Amid slowing financial services activity, it will be interesting to see in what future direction policymakers take the market: one hint may come from the government-funded Financial Services Development Council (FSDC), set up in 2013 as a "high level, cross-sectoral advisory body" to map out a 'strategic direction' for the financial services industry. Its March 2022 paper on enhancing IPO offerings set

the stage for the HKEX consultation on pre-revenue 'specialist technology' companies. More recently, its August 2023 paper, "Enhancing Market Liquidity and Diversity" recommended, among other things, reviewing stamp duty on stock transactions, which was taken on board. Another suggestion it made is to introduce a disclosure-based professional investor-only market: options may soon be destined to thin out for Hong Kong's shrinking pool of retail shareholders.

Judicial efficiency

Being a judge today looks less appealing than in the past

Judicial independence has been a live and thorny topic, particularly against the backdrop of national security cases. We wrote in our last CG Watch of judges being the subject of regular criticism from political figures in Hong Kong and China. While this may have ebbed, in its place there is growing international scrutiny and concern over the ability of judges to act with autonomy and the effect this has had on the Judiciary as a whole. It is something that sits in the background as judges go around their business elsewhere. While it appears to be business as usual in securities and commercial cases, sitting as a judge may appear to be a less appealing prospect for legal minds in Hong Kong these days. The UK government in March 2022 fully supported the withdrawal of British judges sitting on Hong Kong's top court, dubbing the practice as "no longer tenable." There are now just nine overseas non-permanent judges, down from 15 in 2020. And in May 2023, a law was quickly passed to bar foreign lawyers from working on national security cases.

Covid revealed Hong Kong court to be technological laggards

Another issue in recent years has been technological advancement within the Judiciary. When Covid hit, the courts simply closed indefinitely, revealing difficulties in being able to deal with cases any other way than in person. As the pandemic progressed, it forced a reckoning: an old school profession had to adjust to video links and electronic correspondence. We are not quite at the stage of open broadcasts of hearings (although there appears to be a trial run of livestreaming going on at the Court of Appeal), but it is hoped that Covid was a turning point for the profession, which is still paper-heavy and moves slowly (in 2022 the average time between filing a case and getting your first High Court date was 180 days), ever the slave to counsel's diaries.

A new legislature gets to work

The legislative make-up is very different today

In March 2021 the National People's Congress directed an overhaul of Hong Kong's electoral system. Candidates would have to be vetted by a government body, and the number of directly elected seats dropped from 35 to 20 (there are a total of 90 legislative councillors). Today, its demographic is very different from past legislatures. The 20-member Financial Affairs Panel, which oversees issues relating to the financial markets, is chaired by the CEO of a local brokerage firm. Members include the secretary general of the Real Estate Developers Association of Hong Kong and the nephew of the former Chief Executive of Macau. Only three members are female.

A bill on virtual AGMs was able to sail through the legislature

With this change in the legislature, there is a sense that government bills pass much faster, and with much less resistance, than in the past. An example of this can perhaps be seen in the swift passage of an amendment to the Companies Ordinance in January 2023. It took just seven weeks for the bill on virtual AGMs to make it to the statute books (and this was during the Christmas/New Year period), leaving little opportunity for debate or discussion. Indeed, there was no formal consultation and no bills committee was formed, where the merits, principles and ramifications of a draft are put under the microscope and stakeholders are invited to address lawmakers at public hearings, or make public submissions on the proposed changes.

The SFC does not offer independent views on market reforms

The SFC appears to have a broader mandate

One of the questions we ask in CG Watch is if the securities commission is formally and practically autonomous of government. As we explore in our section on Regulators, the SFC has a simple funding model which has historically delivered practical financial autonomy, even if it must have its budget approved by the Legislative Council. The regulator historically had a clearly defined patch, which was market integrity, replete with a broad set of investigative and disciplinary powers. Over the years, the SFC was a more obvious part of the CG community, pushing back on market reforms such as weighted voting rights pre-2018, or pointing out shortcomings worthy of attention (we mentioned Julia Leung's observations about market quality earlier). While it did offer guidance (and somewhat of a different view from HKEX) on separate class rights for H shares in 2023 it appears a less public campaigner of CG today. The SFC has not publicly offered its independent view on any HKEX market consultation or development since 2018. We note that in its recently published strategic plan for 2024-26, the SFC places emphasis on "enhancing the global competitiveness and appeal of Hong Kong capital markets," as its second of four (market resilience remains number one) priorities, which seems much stronger than the duty to 'have regard to' Hong Kong's status as an international financial centre set out in the Securities and Futures Ordinance (SFO).

Changes to H share class rights may make the market less appealing

Connected but not fungible

Hong Kong's stock market has in the past three decades served as a natural destination for PRC companies seeking to raise capital, and its fortunes are very much tied to developments across the border. With the IPO pipeline now tighter controlled by Beijing (see our chapter on China) the extent of the role Hong Kong will play as a fundraising centre for companies based in the hinterland looks less clearcut. It is now setting its sights further afield for IPO candidates, including Southeast Asia and the Middle East. Meanwhile the H share market, which turned 30 in 2023, may lose some of its appeal to investors after the Stock Exchange announced the disbanding of separate class votes for holders of these shares when it comes to variation or abolition of their rights, including dilutive rights issues. HKEX claimed a change in PRC regulations required such a move, and that there should no longer be a distinction between the two (although this came with caveats). ACGA and investor groups argued that the shares are distinct because they are not fungible. The SFC seemed to agree. The Exchange sought market views on whether this would impede further development of the H share market: the response from investors was a resounding yes. H share companies traditionally trade at a much higher discount to their A share counterparts: this A/H divergence is tracked daily and the premium hit a five-year high in January 2024.

Class actions and alternative fee structures for litigation are still off the table

A familiar story on shareholder recourse

It has increasingly been a feature of Hong Kong's stock market that most companies are incorporated overseas (only around 8% are incorporated here), making it cumbersome to enforce shareholder rights, and in the worst scenario, wind up the issuer. Shareholder battles are more likely to be fought in the courts of the Cayman Islands than those in Hong Kong for geographical reasons, but investors contemplating a claim for unfair prejudice or a derivative action within the jurisdiction are few and far between. The legal hurdles are high and the costs prohibitive. Hong Kong raised our hopes somewhat that the reform might still be in play to create a more conducive landscape for shareholder litigation: in December 2022 it allowed outcome-related fee structures in arbitration and arbitration-related court proceedings. This is one of the few Law Reform Commission recommendations to see the light of day in recent years. The new regime allows alternative fee structures, including no win, no fee arrangements. Sadly the

opportunity was not taken to revisit the topic of loosening Hong Kong's tough rules on fees for shareholder lawsuits: you can still go to jail for up to seven years for funding someone else's litigation and taking a share of the spoils, something the UK abolished 57 years ago. Likewise, no progress has been made on class action reform, something that was first recommended by a working group led by the Chief Justice back in 2004. We wrote about this at some length in our 2020 CG Watch report: there is no progress to report.

The ICAC turns 50

The private sector keeps the anti-corruption agency busy

Hong Kong has come some way to quash its crude, post-war corruption plight which led to the establishment of the Independent Commission Against Corruption (ICAC) in 1974. It has a reputation for a clean civil service and judiciary, a city where laisee (red packets of cash) only come out as a token gesture, annual tip or generous wedding gift, and backhanders are generally the exception rather than the norm. A hyper vigilant public diligently alert investigators to malfeasance given the ICAC's strong emphasis on education. There are bad apples - a number of senior figures, including a former chief executive have been ICAC scalps in the past - but by and large the anti-corruption agency's caseload is very steady year to year and relies on the private sector to keep them busy. In 2023 the ICAC dealt with 1,566 pursuable corruption complaints, an increase of around 9%. There were 79 pursuable election-related complaints (the ICAC enforces the Elections (Corrupt and Illegal Conduct) Ordinance as well as the Prevention of Bribery Ordinance), also an increase of 9%. At the end of December 2023, it had a total of 969 ongoing cases on its books. Private sector complaints accounted for 72% of the total, with those relating to government departments and public bodies standing at 23% and 6% respectively. Most private sector cases originated from the building management, finance, insurance and construction industries.

Most corruption complaints are spin-offs of a wider deception

Excluding election offences, there were 204 people prosecuted following an ICAC investigation in 2022 (figures for 2023 could not be found) and the majority of these were not for corruption per se, but those 'connected with or facilitated by corruption and specified offences.' Most involved deception under the Theft Ordinance. A total of 60 people were prosecuted for bribery offences. In terms of outcomes, 165 of all the prosecutions are still outstanding: in 2022, 36 people were convicted and nobody was acquitted. Sixteen cautions were given. There have not been any blockbuster cases of late, typical examples range from small change to more pervasive, sophisticated syndicates.

Hong Kong lags Singapore on corruption perception

Perception is another issue. Hong Kong comes off worse than Singapore in terms of how corrupt people think it is. In Transparency International's 2023 Corruption Perceptions Index (CPI), Hong Kong ranked 14th place (Singapore ranked 5th). The CPI incorporates views from institutions and experts in the city, as well as other surveys. Transparency International in the past has cited Hong Kong's shortcomings in beneficial ownership transparency and cross-border corruption, as well as a business environment "where shell companies and corruption can flourish.'' It seems this was reinforced by the findings of the International Consortium of International Journalists (ICIJ) resulting from the Panama Papers leak in 2016. Hong Kong was revealed to be a major player in the global network of offshore financial centres, which are used to manage both legal and illicit financial flows. Hong Kong further came under criticism for obfuscating director details on the companies register in 2021 and generally making it more burdensome to do get any corporate information: having to fill in a form with the Companies Registry giving your personal details and providing reason for the search now comes with a significant risk, as journalist Bao Choy found out (see our section on Civil Society and Media).

The ICAC is very well resourced to deal with its caseload . . .

The anti-corruption agency is amply funded from the general reserve, with an estimated budget of HK$1.38 billion for the 2024-25 financial year of which HK$1.08 billion is earmarked for operations (actual spending on operations in 2023-24 was HK$1.06 billion.) Staff in the operations division number 1,226 of a total 1,575. Operations is the investigative arm of the ICAC.

2. Regulators

Hong Kong ranks joint 5th with Singapore on a score of 62%

Hong Kong dropped from 1st to 5th place in this category, with an overall score of 62%, a loss of seven percentage points compared to 2020. It now ranks slightly behind Australia, Japan and Taiwan (who scored 65%-66%) and Singapore (63%). Much of the decline can be laid at the feet of a reform agenda in the past years which in our view has prioritised IPO volume over quality of the market.

The market is a tale of two regulators

The SFC focusses on keeping bad actors out of the market where possible (its 'frontloading' or Minority Report-style approach is to cut off nefarious transactions and IPOs before they enter the public domain) and it pursues market miscreants under securities law once they slip through the net. HKEX's role as frontline regulator of the listing rules meanwhile remains overshadowed by its conflicting drive to maximise profits. It metes out limited sanctions, although these have been ramped up in recent years to include unsuitability statements (in other words, the directors are deemed not fit to run the listed company). But a progressive theme to emerge from both regulators is the role that cross-border reality plays in both the nature of action that can be pursued against directors or other bad actors, and the result that can be achieved. If a director who resides in China decides to evade service of SFC papers, even with the help of PRC securities regulators, there is not much to do. All too often companies subject to fraud, false accounting or other misconduct on the part of its directors fade into the prolonged suspension list and eventual delisting, with shareholders ultimately left empty-handed.

2.1 Funding, capacity building, regulatory reform

Hong Kong falls from 1st to 6th place on score of 54%

Hong Kong dropped from 1st to 6th place in this sub-category on a score of 54%, losing eight percentage points compared to 2020. It was a narrow race and Hong Kong only ranks behind Singapore and Malaysia by just two points. The biggest drag on the score reflected HKEX's programme of market reform in the past few years, which has been to pursue quantity of listings. With each new regime for overseas issuers, or specialist tech firms and SPACs, comes a gradual chipping away of fundamental protections for shareholders. It all adds up, particularly as no such effort has been put into levelling the playing field for minority investors. On the capacity side, the SFC has been through a rough patch with a brain drain and loss of junior professionals (HKEX does not disclose its funding for regulation).

Funding the SFC and a $96 billion question

Market volatility is impacting the regulator's levy funding

Hong Kong's securities regulator remains one of the best-funded in the region and its coffers benefit from a simple 0.0027% levy on transactions (accounting for 88% of funding), which has not been raised since 2014. This traditionally sees it remain comfortably in the black, with a deep pool of reserves. While there is a provision in law for the government to fund the SFC if needed, there has been no such request since the early 1990s.

Income has dropped and the SFC is in deficit, but with a respectable reserve

The SFC's total income in 2022-23 was HK$1.9 billion, a drop of 14% from the previous year as market volatility took hold. Levy income fell 19% to HK$1.7 billion. Compare this with 2020/21 when overall income was up at HK$3 billion - the SFC has kept expenses at around HK$2 billion a year, but its surplus of HK$979m in

2020/21 has since slipped to a deficit of HK$101m in 2022/23. As of 31 March 2023, the SFC's reserves stood at HK$7.9 billion, with HK$3.4 billion put aside to go toward new premises: in November 2023 the regulator purchased 12 floors at the One Island East office block for HK$5.4 billion from Swire Properties, with payments to be staggered through to 2028. Its total reserves available for daily use as a result for 2024-25 were estimated to be HK$3.9 billion.

The SFC struggles with staff departures during the pandemic

Staff costs at the SFC hover at around 75% of its expenditure, in 2022/23 dipping to 74.5%. The summer of 2022 was a low point for SFC human resources: half of the six executive slots at the regulator, including that of the CEO, were soon to be vacant. Ashley Alder had just announced his resignation as CEO, cutting his term short by nine months to join the UK's Financial Conduct Authority (FCA). The SFC's executive directors of enforcement and corporate finance had departed the previous May and August. They joined 12% of the SFC's employees who headed for the door in 2021, including 25% of its junior professionals. A manpower squeeze led to a warning by the regulator that its work was being impacted. On-site inspections of listed companies declined to 200 in the 2022-2023 year, which the regulator said in a Legislative Council briefing was decidedly short of its 300 target.

The securities regulator finds a new CEO from within . . .

The regulator promoted from within, appointing Alder's deputy Julia Leung Fung Yee as CEO from 1 January 2023. Ms Leung first joined the SFC in 2015 after being Under Secretary for Financial Services and the Treasury and serving at the Hong Kong Monetary Authority. The regulator also moved Michael Duignan from enforcement back to corporate finance to head up the unit, while a former general counsel at HSBC, Christopher Wilson, would take charge of the enforcement division in November 2022. As for the rest of the headcount, according to its briefing to the Legislative Council we know that the SFC is underspending in part due to a 'time lag in filling vacancies,' but no new bodies will be added in 2024/25. Its headcount will remain at 1,022. This is up from its pre-pandemic figure of 988. In the SFC's latest annual report, as of March 2023 there were 1,018 staff budgeted for (838 of these are from the professional ranks), but the actual headcount was 933, leaving a shortfall of 85. The shortfall for 2022 was 75, while as of 2021 it was 55.

. . . as does the Stock Exchange

Meanwhile over in Central, the for-profit listed company which also acts as frontline regulator of listed companies, Hong Kong Exchanges and Clearing (HKEX), has had a few staff changes of note. Former JP Morgan banker Nicolas "Gucho" Aguzin announced in December 2023 that he would not seek reappointment as CEO, and decided to speed up the process by departing a few months shy of the end of his contract in February 2024. Again, promoting from within, Co-Chief Operating Officer Bonnie Chan Yiting was appointed CEO effective 1 March 2024. Meanwhile, government-appointed chair of HKEX Laura Cha Shih May Lung stood down in April 2024 and was replaced by Carlson Tong, a former KPMG chair who previously held the position of SFC chair between 2012 and 2018.

Funding the frontline regulator (and lots of questions)

There is no disclosure on how much the Exchange spends on regulation

HKEX revenues have been under pressure given the current state of the stock market and a slowdown in IPOs. Revenue in 2022 was down 12% to HK$18.5 billion and profits slumped by 20% to HK$10.1 billion. HKEX results for 2023 show an improvement: profit was up 18% to HK$11.6 billion on revenue of HK$18.9 billion, a 3% hike on 2022. A key driving force was growth in its derivatives, fixed-income and currencies business. Average daily turnover of equity products was down 14% to HK$93.2m. HKEX does not provide details on its enforcement budget or staffing.

Its annual report only states that costs associated with frontline regulation "are absorbed by the cash and equity and financial derivatives segments in proportion to the listing fee income of the two segments." There is no indication of more spending on enforcement. We know in 2022 it did spend 13% more on staff costs, but additional headcount was for "strategic initiatives." Another area worthy of more budget was marketing and promotion, which received an 11% boost - including cash incentives relating to new products during the year.

Regulatory reform and risky business

SFC reforms focus on takeovers, virtual assets

Much of the reform to come from the SFC on the CG front of late has been of a tidying-up nature, including the September 2023 consultation conclusions on changes to the takeovers and share buy-backs codes. Where it has weighed in heavily is on virtual assets, as Hong Kong maps out a tighter regime and enforcement given the growing participation of retail investors. In an October 2023 survey by the Hong Kong University of Science and Technology, more than 25% of respondents said they hold virtual assets. In March 2023, the SFC licensed two virtual asset trading platforms after legislation was passed in December 2022 to bring the crypto space under its formal purview.

A new identification regime is introduced for trading

A new investor identification regime was launched by the SFC in March 2023, and September 2023 saw the introduction of a reporting framework for over-the-counter (OTC) securities transactions. The identification requirements were aimed at overcoming surveillance issues when monitoring suspicious trades, with the SFC previously required to obtain information on investors' brokers. HKEX's trading system only captured the securities order itself, not the ultimate client instructing it. Brokers must now provide client identities (name, identity/passport number) to a data repository with the Stock Exchange. The December 2020 consultation carried out by SFC ahead of introducing the new regime ring-fenced reform to the trading level disclosure only - there was no plan to extend it to cover investors' holdings.

HKEX reforms underscore a mission to boost listings

HKEX meanwhile moved ahead with market reform focussed on generating IPOs. Having introduced weighted voting rights (WVR) in 2018, it has since given us SPACs, a broader secondary listing regime with a very generous waiver culture, a new framework for overseas companies' core listing requirements which lowers the bar below Hong Kong company law, and most recently the introduction of zero-revenue tech firms. Bar the increased diversity of offerings for investors, we did not see much upside by way of greater protections, or major upgrades to the CG rulebook, to level the playing field. While HKEX took the quasi-quota route with a requirement for no single gender boards by 2025, it backed down on significant reform to INED tenure. In 2023, the Exchange also changed the listing rules to strip holders of H shares of separate class votes where their rights are to be altered or subverted. In June 2024, HKEX began a consultation on changes to the CG Code and Listing Rules, which has opened the door to potential reform on INED tenure and overboarding, and the notion of a Lead INED. The consultation runs until 16 August 2024.

Secondary listings receive a pass on key CG rules

Secondary listings receive a free pass on most of the core CG elements of the listing rules and the takeovers code on the supposition that they face similar regimes in their primary listing market. Most of the large PRC firms who account for the lion's share of secondary listings are however primary listed in the US, which allows them to defer to the rules in their country of incorporation, which is usually the Cayman Islands or BVI. A large group of secondary listings (the likes of Alibaba, JD.com and NetEase) accounted for a sixth of Hong Kong's total market cap, but received

automatic waivers on notifiable and connected transactions, the CG Code, ESG reporting requirements and so on. HKEX automatically grants 77 waivers to secondary listings. JD.com only held its first AGM in 2021, seven years after it listed in the US. But Hong Kong in November 2021 concluded that, to take advantage of "homecoming" secondary listings (PRC firms already listed in the US) it would further ease barriers to entry. These firms were given more generous wiggle room on new "Core Protection Standards'' for overseas issuers, including longer notice for AGMs and general meetings. While companies incorporated in Hong Kong who follow the local company law and the CG Code must give 21 days for an AGM and 14 days for other meetings, secondary listings need only give "reasonable" written notice (although 'normally' this would follow the Companies Ordinance requirements above). It also became tougher for shareholders of secondary issuers to convene a general meeting: the Companies Ordinance requires 5% but these overseas listed companies get a more generous 10%. Practically speaking, even obtaining 5% in Hong Kong is a major task given the dominance of significant shareholders. There was also some flexibility for some of these Core Standards to be applied on a case-by-case basis.

Hong Kong comes late to the SPAC party

In December 2021, HKEX concluded that the time was ripe for blank cheque companies. The rulebook they came up with avoided some of the more rogue elements of traditional blank cheque firms, and was open to professional investors only. To date, this particular market development has hardly seemed worth the effort: to date, Hong Kong has just five SPACs.

Zero revenue tech firms can now list on the main board, but we cannot find any

In the third quarter of 2022 and the Exchange sought to reverse its fortunes by bringing in a new regime for fledgling tech firms. Such "leading edge" tech firms (which would treat makers of electric vehicles and fake meat alike) could IPO with zero revenue but "high growth potential.'' Extra comfort for investors would be in the form of the "sophisticated investor'' who would have to invest ahead of an IPO: the major financial backers in effect became a proxy for suitability of a listing. These firms were able to list from 31 March 2023 but, to date, we have not noticed any such listings.

Weighing up dual class stocks

Hong Kong's first dual class listing has had a bumpy ride

Hong Kong's score took a hit in our last CG Watch with the introduction of dual class shares (or weighted voting rights as they are known there). There are now 22 companies with WVR listed in Hong Kong, and six of these are currently included in the Hang Seng Index (which comprises 82 companies in all): Xiaomi, Li Auto, Meituan, JD.com, Baidu, and Alibaba. Three of these are secondary listings; there are an additional two issuers with a primary listing elsewhere, Trip.com and NetEase. The HSI has dropped by 43% over the past three years dragged by these tech names. Alibaba, the company Hong Kong policymakers wanted to list and the catalyst for a dual class share regime has been caught up in a general crackdown on tech in China, its founder Jack Ma saw his star fall after being critical of market policy in the PRC and for a number of years his whereabouts were something of a mystery. Meanwhile as Jack Ma claims to have stepped away from the company, he remains not only a partner of the Alibaba Partnership, but one of its "partnership committee continuity members,'' along with Joe Tsai.

Market consultations are often very long

Regulatory consultations

One of the new questions we added to our last CG Watch was whether public consultations are undertaken on regulatory matters and in particular that these go beyond a rubber stamp exercise. Hong Kong lost ground here. HKEX consultations can be very long and ask for yes/no responses to set questions on a topic with reasons why these have been given in an online questionnaire. There is no actual person or email address provided (although we still do send an email with our submission to HKEX). The exchange tends to use percentages to justify a course of action.

The rise and fall of a Hong Kong company raises some questions about the market's IPO strategy

The founder, his wife, the son and Mr Un

If there was a consistent theme among policymakers in Hong Kong over the past few years has been that every small to medium-sized enterprise should list on its stock market. But is tapping the capital markets really for everyone? The rise and fall of Sun Cheong Creative Development suggests not. This was a quintessentially Hong Kong family business. Set up in 1979, Sun Cheong had its headquarters in Hong Kong, factories in China and major customers in Australia, the UK, New Zealand and the US. It made "stylish, reliable but affordable'' plastic food containers under the "ClipFresh" brand which it sold to supermarkets and department stores.

The company listed after 40 years and when the founders were retiring

The company decided to go public nearly 40 years later in October 2018 when its founder Tong Ying Chiu and his wife Sylvia Ng Siu Kuen (who was also a director) were both retirement age. Their son Billy was also on the board as CEO. At the time, the company was turning a respectable profit of HK$33.8m (US$4.3m) on revenue of HK$341m (US$43.6m) and it employed 452 people in Hong Kong and China. The IPO raised HK$97.7m (US$12.5m) and Sun Cheong put some of the money into new plastic moulds.

It imploded within 15 months of the IPO

Within 15 months, there was bedlam. The founder and his wife who held 50.05% of the issuer abruptly quit the board in December 2019 (and took some of the books and records with them) and nobody was paying its factory workers. By January PRC authorities had stepped in and sealed off the factory. Shortly after, the unpaid employees grabbed accounting records and held them as ransom. The company then cited Covid as a reason for the delay in publishing its 2019 financial results and when they eventually emerged in July 2020, it was subject to an auditor disclaimer. This referred to a number of issues, including the inability to obtain the books and records of Sun Cheong's PRC subsidiaries. Trading was suspended and the stock was de-listed in May 2022. HKEX sanctioned the founder, his wife, their son and executive director Un Ge Wei in November 2023 for misleading investors in their disclosure, deeming them unsuitable to be directors.

It is a familiar legacy that public shareholder face

Sun Cheong's experience as a listed company was as crash and burn as they come, which is not unheard of among Hong Kong's stock picks, but few of these have a 40-year track record.

Hong Kong is equal 1st with Australia based on a score of 72%

2.2 Enforcement

While Hong Kong maintained its top position in this category, sharing 1st place with Australia, it did so on a lower score of 72%, down four percentage points from 2020. Conversely, Australia narrowed the gap between the two markets with a gain of four percentage points. Hong Kong is no longer comfortably ahead of Singapore, which scored 71%.

Conflicts at HKEX and market misconduct results are a drag on the score

There are 10 questions in this category and Hong Kong lost points for two of them: we cut a point over the management of conflicts of interest at HKEX as a for-profit exchange. We also took off a mark for enforcement of market misconduct. Part of this reflects the difficulties the SFC faces in pursuing bad actors who evade action when they vanish across the border. But we also wonder about the time lag in pursuing cases, particularly at the Market Misconduct Tribunal (MMT) where things move at a very slow pace.

The for-profit exchange continues to be dogged by conflict concerns

A conflicting picture

In our last CG Watch we wrote about the SFC's 2019 review report on HKEX's regulatory performance, which highlighted conflict of interest shortcomings in the pre-IPO process as well as weak Chinese walls between the listing department and the business division.

The SFC is still flagging issues with information sharing between divisions at HKEX

Fast forward to 2023 and it seems the securities regulator still harbours concerns over potential conflicts of interest. It made the point of stressing that HKEX put procedures in place "to ensure that non-public listing-related information be kept confidential from personnel outside the Listing Division." The SFC drew attention to the fact that the Listing Operation Governance (LOG) Committee set up in June 2021 to help the HKEX board oversee management and operations of the listing division invited the exchange's chief risk and compliance officers as well as its general counsel to meetings on a regular basis. This means they receive "certain non-public listing-related information," despite not being LOG members themselves.

An advisory body to the HKEX board is supposed to consider the public interest . . .

Equally concerning is the SFC's assessment of how the LOG Committee conducts itself. Here is a committee specifically set up to enhance oversight of the listing regulatory function: HKEX is a for-profit exchange, but by statute it has an obligation to act in the public interest, and ensure these interests prevail where they conflict with those of HKEX. The board has a duty to supervise HKEX in performing its statutory duties, and the LOG Committee is supposed to help them do this. Its terms of reference provide that the committee should review any major listing policy changes put forward by the Listing Division and give guidance on how this is to be balanced with the public interest obligation. Five people sit on the LOG Committee: three non-executive directors appointed by the HKEX board and the chair and a deputy chair of the Listing Committee, who are not HKEX employees.

. . . but it takes its cue from the Listing Division

Poor record-keeping at the advisory body is an issue

Things did not get off to a great start in 2021 as the LOG Committee took a different view on its function. On listing policy matters, it decided it should not try to replace the role of the Listing Division or Listing Committee where public policy interests were concerned. Instead, it should focus on "specific aspects" identified by the Listing Division. And in 2022 what transpired was the Head of Listing verbally reporting to the LOG Committee the public interest considerations as the Listing Division and Listing Committee saw them. There was no record in the meeting minutes of any guidance or comments the LOG Committee had on the public interest implications. Nor did HKEX board minutes contain any reference to LOG Committee advice to the board on these.

The committee tasked with advising the board is more concerned with due process

The explanation the SFC received was that discussions did not revolve around substantive issues at LOG meetings, but whether governance and due process had been observed when listing policy initiatives were developed, and whether the Listing Committee had duly deliberated them. But some LOG members had raised questions on public interest considerations on some market consultations. Still, the SFC stated that the LOG Committee has only been operating for a short time and its "track record has yet to be developed." It did however suggest that keeping more detailed minutes of LOG meetings might be a wise idea.

The rise of the unsuitables

More directors are found to be unsuitable by HKEX

In July 2021 HKEX saw its disciplinary powers and sanctions expanded to include a director "unsuitability statement". If HKEX deems a director unsuitable to serve as such, or as senior management, the expectation is that the issuer will remove them. If not, further action can be taken, including denial of market facilities. In 2023, 29 unsuitability statements were issued, more than double that of 2022. It is interesting to note that one sanction in Figure 11, the prejudice statement, has seen less activity in 2023, suggesting such cases in the past would have warranted a more severe reprimand had it been available.

Here is the range of sanctions imposed on directors and issuers

Figure 11

Rogues gallery: sanctions imposed by the Hong Kong Stock Exchange, 2021-2023

HKEX Enforcement Sanctions	2023		2022		2021	
Nature of sanction	Issuers	Individuals	Issuers	Individuals	Issuers	Individuals
Unsuitability statement		29		13		na
Prejudice statement		22		29		56
Public censure	17	42	17	40	20	84
Public statement involving criticism	1	22	5	57	5	43
Private reprimand	1	9	1	28	0	12
Internal control review	4		4		6	
Appointment of compliance advisor	2		1		2	
Director training		78		117		120
Regulatory letters	16	89	24	65	10	48

Source: www.hkex.com.hk

Among the 'unsuitables' are a number of INEDs

2023 was a busy year for unsuitables and among them are a fair number of independent non-executive directors (INEDs). In June 2023 two former INEDs at China Clean Energy Technology Group were subject to an unsuitability statement after they ignored a shareholder requisition (and eventually a court order) to remove the board of directors at an EGM. The pair were found to have improperly resisted the shareholder vote to remove them from office and failed to cooperate with the HKEX investigation. An INED at Jilin Province Huinan Changlong Bio-pharmacy Company likewise was subject to an unsuitability statement in June 2023 (a further six executives, including the chair, and two INEDs only faced a criticism) after persistent failure to disclose notifiable transactions. The INED in question, Gao Yong Cai, had failed to respond to HKEX enquiries. In April 2023, INED Dr Hu Xu Dong at S&S Intervalue China was deemed unsuitable after the company lost close to RMB200m as a result of unauthorised loans to third parties. Meanwhile three INEDs at China Gem Holdings in February 2023 were found to be unsuitable after failing to respond to HKEX enquiries. There are a significant number of cases where other INEDs faced a rebuke. In October 2023, four

former INEDs at China Fortune Holdings were criticised for failing to keep on top of connected transactions via its subsidiaries. Despite a warning in 2018 from HKEX they took no steps to improve internal controls.

HKEX has also been giving INEDs private rebukes

Also of note are the nine private reprimands issued to directors during 2023. Although these remain anonymous, HKEX does provide a summary each year which gives an outline of the breaches in question. In the examples given, five INEDs were given a rap on the knuckles. Two of them had not bothered to ask for monthly financial or business updates (and it turned out that the company agreed to pay out more than half of the IPO proceeds to third parties, but failed to disclose this in the listing document). In another case, a sub-placing agent controlled by two executive directors received more than 90% of the placing fees. The directors were reprimanded for conflicts of interest.

Nothing to see here?

HKEX is moving a lot faster to delist delinquent issuers . . .

In the past HKEX has faced some criticism about its delisting process and the speed with which it shows issuers the exit when they fail to publish financials, hold AGMs, or there has been fraud or other financial irregularities which the company cannot fix to the satisfaction of regulators. To give credit to the Exchange, this state of affairs appears to have been addressed, not without some kicking and screaming on the part of issuers who have taken them to court on several occasions (and lost) to try to salvage their listings. Still, there is no shortage of candidates: as of the end of February 2024 there were 56 main board companies on the prolonged suspension list (not without a touch of irony, the longest-suspended company is China Longevity Group, which was suspended in February 2013) and a further 17 on the Growth Enterprise Market (GEM).

. . . but some are crashing and burning very quickly

For the year ended 31 December 2023, 34 long-suspended companies on the main board were delisted and the figure for GEM companies was 10. So for the main board, that was nearly three a month. While it is good that things are moving faster, some of these issuers had a very short shelf life. It does beg the question as to the desirability of some of these listings in the first place when they are so quicky shuffled out of the door: take the example of magnetics parts manufacturer Universal Star (Holdings) whose listing was cancelled by the Exchange on 24 January 2024. The company raised HK$125m at IPO in May 2019. It failed to publish its 2021 annual results and the stock was suspended from trading in April 2022. There is no trace of it in HKEX's depository of company announcements so why its star crashed so quickly is anyone's guess.

Investment scams and ramp and dumps are keeping the SFC busy

They still jail insider dealers, don't they?

As with many regulators in the region, the SFC keeps occupied with a mix of traditional market misconduct (from price rigging to illegal short selling) and whatever mischief is putting investors at risk. In recent years, it has been investment fraud and social media-related ramp and dump schemes, drawing the securities regulator into joint operations with police and the anti-corruption agency. In the social media ramp and dumps, investors are enticed to buy in before the culprits dump at an artificially-high price. The SFC, in its latest annual report, identifies these schemes as an enforcement priority, and we note the first criminal ramp and dump case began at the District Court in February 2024. Two defendants have been charged with the somewhat unwieldy offence of 'conspiracy to employ a scheme with intent to defraud or deceive in transactions involving securities.' The case has been adjourned until April.

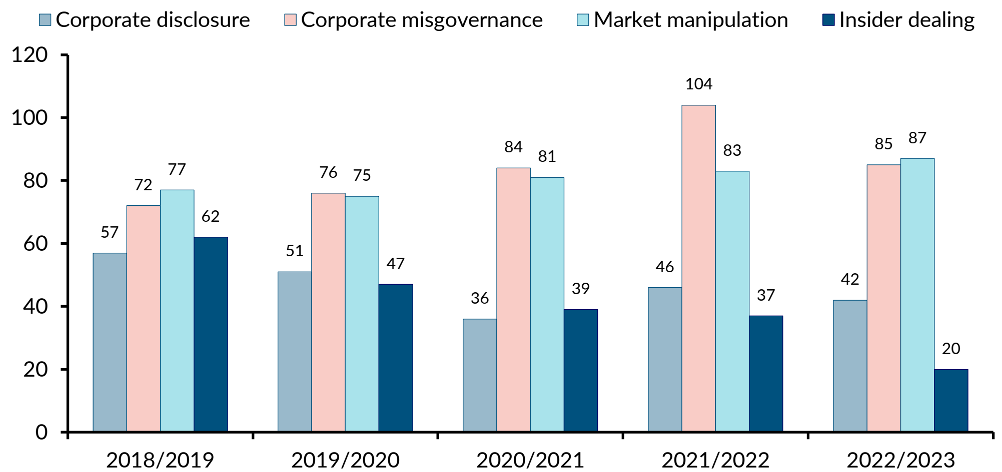
Insider dealing cases are sparse

Meanwhile, the number of investigations into insider dealing has dropped significantly, with cases barely a third of what they were three or four years ago. According to the SFC's latest annual report, there were no criminal prosecutions for insider dealing in 2022 or 2021 and just one in 2020. Perhaps Hong Kong has cleaned up its act on this front but nor is it a wrongdoing which attracts much attention these days as civil cases traipse their way through Hong Kong's Market Misconduct Tribunal (MMT). Since our last CG Watch, only one insider dealing case has been referred to the MMT (with the relevant trades dating back to 2017) and one was concluded.

Insider dealing investigations are in significant decline

Figure 12

SFC investigations into market misconduct, 2018-2023



Source: SFC annual report 2022-23

There have been some criminal prosecutions for market offences

The SFC's 2023 annual report sets out successful prosecutions (for all market misconduct involving fines of HK$10,000 and above) in 2022, of which there were five, including a two-and-a-half month jail term for Danny Fung Kwong Shing in October that year for manipulation, and three cases of illegal short selling, all of which attracted fines. In one case, the SFC's costs were higher than the fine itself. Another criminal case saw Wong King Hoi given two weeks' imprisonment for obstruction.

These are the key trends in enforcement by the SFC

From the SFC's enforcement figures, a few notables to assist in navigating the table in Figure 13: there have been fewer compliance letters in what seems to be an ongoing trend. But more people have been summonsed for criminal proceedings (non-insider dealing and market manipulation) than in previous years, albeit only 10 cases. Section 179 inquries empower the SFC to compel the production of records and documents from a person related to a listed company where there is suspected fraud or misconduct: these have gone from a high of 57 in 2021/22 to just 31 in 2022/23.

This is the picture of enforcement by the securities regulator

Figure 13

Where is the SFC putting its enforcement efforts? 2020/21-2022/23

SFC enforcement activities	2022/23	2021/22	2020/21
s179 enquiries commenced	31	57	42
s181 enquiries commenced (number of letters sent)	191 (5,851)	203 (7,308)	246 (8,748)
s182 directions issued	130	214	189
Rule 8 directions issued	0	0	0
Insider dealing:			
Individuals/corporations summonsed (summons laid)	0 (0)	0 (0)	1 (1)
Individuals/corporations involved in ongoing civil proceedings	8	8	11
Individuals/corporations involved in ongoing MMT proceedings	2	2	3
Market manipulation:			
Individuals/corporations summonsed (summons laid)	1 (25)	0 (0)	6 (6)
Individuals/corporations involved in ongoing civil proceedings	18	18	18
Individuals/corporations involved in ongoing MMT proceedings	1	0	0
Others:			
Individuals/corporations summonsed (summons laid)	10 (73)	4 (28)	3 (21)
Individuals/corporations involved in ongoing civil proceedings	154	142	150
Individuals/corporations involved in ongoing MMT proceedings	11	11	11
Individuals charged for suspected market misconduct and money laundering offences for indictment prosecution	14	0	0
Disciplinary enquiry			
Notices of proposed disciplinary action issued	26	37	27
Notices of decision issued (including s201 agreement)	29	43	35

Source: SFC annual report 2022/23 Note: **Section 181** inquiries is where the SFC can require information from intermediaries about trading transactions; **Section 182** is a broad power to investigate offences under the SFO; **Rule 8** is where the SFC can direct the Stock Exchange to suspend trading in the shares of a company on grounds that the market is misinformed, disorderly or unfair; **Notices of proposed disciplinary action** informs a regulated person that the SFC plans to exercise its disciplinary powers; **Notices of decision** sets out a decision of the SFC and why it is taking disciplinary action; A **section 201 agreement** is where the SFC resolves disciplinary proceedings by agreement.

The great escape

Taking action against directors in China is a difficult task

One distinct theme to emerge from reading individual cases of SFC enforcement action (and court cases) over the past few years is that pursuing directors who disappear across the border rather than face the music is an arduous and often futile task. Much like the SFC's decision to focus on a frontloaded approach to supervision (taking pre-emptive action against issuers as market irregularities become apparent), several of the SFC's enforcement cases of late reflect a pragmatism in getting the best result it can in the circumstances, even if it is not the most satisfying one.

The SFC has been taking action to order directors to buy out shareholders

A good example can be found in the October 2022 ruling by the High Court at the SFC's request that the chairman and controlling shareholder of PRC-based wastewater treatment firm Sound Global Wen Yibo buy out shareholders after he fabricated bank statements to grossly inflate the company's balances by RMB2.18 billion in 2012 and RMB2.72 billion the following year. He was also barred from being a director for 12 years. It was the first compensation order of its kind made under section 214 of the Securities and Futures Ordinance (SFO) which enables the regulator to force errant directors to buy out shareholders and disqualify them for

up to 15 years. Given the company had been suspended from trading since 2016 (and has subsequently been de-listed) it at least gives shareholders something back. All too often prolonged trading suspensions result in shareholders receiving nothing when the company's listing is eventually cancelled by the Exchange. The judge concluded that 12 years was an appropriate ban given the "very serious nature of the conduct, which involved fraud and dishonesty on the part of Mr Wen."

The regulator can only take action against directors it can serve papers on

But Wen was the only director to face the music: three other directors dodged sanction because they were in the mainland. The judge noted it was a "paradigm example where the directors of a listed company were able to avoid the enforcement action taken by the SFC by choosing to stay out of the jurisdiction." Serving process in China takes months, if not years, and is futile when deliberate steps are taken to avoid being served. Despite repeated attempts to effect service (and the help of the China Securities Regulatory Commission), the petition was not served on the respondents and the SFC decided to proceed with the trial against Wen and the company only.

The SFC seeks to disqualify an INED amid an accounting fraud

Another section 214 case resulted in Nicholas Chiu Sai Chuen, former INED at GEM-listed China Candy Holdings, being banned as a director for three years in December 2023. Although not involved in the day-to-day business of the company, Chiu was found to have acted negligently after directors fabricated bank and accounting records to cover up inflated cash and bank balances by 87% and 97% respectively in 2016. He admitted failing to uncover the overstatements and neglected to pay attention to red flags in the company's treasury, cash management and financial reporting functions identified by an internal control consultant engaged by the company.

3. CG rules

Hong Kong remains in 4th place on a score of 75%

Hong Kong remained in 4th place in this category, equal with Taiwan, scoring exactly the same as 2020 (75%) when it tied with Singapore. Its rival has since moved up to 3rd place on a score of 77%, narrowly pipped by Malaysia (79%) and more substantially, Australia (83%).

The market has a solid rulebook but one that could be much bolder

The big picture is that Hong Kong had hit a plateau with its CG rulebook: like many markets in the region it has a credible report card on the fundamentals, such as corporate and financial reporting, disclosure of substantial ownership and price-sensitive information, and related-party rules. The CG code gets tweaked every few years, but generally Hong Kong has fallen behind many of its peers in terms of board diversity, caps on long-tenured INEDs and independence. Hopefully this will be addressed: on 14 June 2024 HKEX released a consultation paper on proposed changes to the Listing Rules and CG Code. Among the changes mooted are a nine-year cap on INED tenure, overboarding being capped at six directorships and the introduction of a lead INED where the chair and CEO are not separate:

- A nine-year hard cap on INED tenure with a three-year transition period, making the listing rule effective from 1 January 2028. Long tenured INEDs could be a NED after this. Long serving INEDS would be allowed to serve again as INED on board of same issuer after a two-year cooling off period.
- A new listing rule imposing a hard cap on overboarding: an INED must not concurrently hold more than six listed company directorships. There would be a three-year transition, with the rule coming into effect from 1 January 2028.
- A CG Code provision requiring companies to have at least one director of a different gender on the Nomination Committee.

- A new listing rule would require mandatory director training annually on specified topics. First-time directors would undergo a minimum 24 training hours within 18 months of their appointment.
- Upgrade the current recommended best practice to a CG Code provision that there be a board performance review to be conducted at least every two years on a comply or explain basis, following the UK, Singapore and Australia. The review would consider the board, rather than individual directors.
- A CG Code provision requiring a board skills matrix with enhanced disclosure on the current mix of skills and further ones they are looking for. Issuers should refrain from simply listing out director qualifications and experience.
- A new mandatory disclosure rule that the Nomination Committee must annually assess and disclose its assessment of each director's time commitment and contribution to the board.
- Upgrade the current CG Code provision to mandatory disclosure that companies disclose specific information on their dividend policy, or why they do not have one, as well as dividend decisions made by the board, in the CG report. Issuers should disclose why there has been any variation in dividend rates, and reasons for not paying a dividend.

Long live the INED

Issuers are given three years to get one woman on their board

There was one review of the CG Code since 2020 (a consultation in April 2021 on both the code and the listing rules with conclusions published in December that year), in which Hong Kong called time on single gender boards as a listing rule (issuers have until the end of 2024 to comply) and required anti-corruption and whistleblowing policies from the financial year starting January 2022. Issuers must disclose numerical targets and timelines for gender diversity at the board level and across the workforce, and review its diversity policy annually. Many of these policies are boilerplate and issuers appear to have challenges in developing targets and timelines: some feel that one woman is enough and meets the company's diversity goals.

HKEX backs down on an independent shareholder vote for INED tenure

In the same consultation, HKEX backed down on board renewal, shelving a proposal for a separate vote by independent shareholders on INEDs serving more than nine years on the board (we hope this will change following the June 2024 consultation). Instead it opted for additional disclosure as to why the long-tenure candidate should be re-elected, and a new code provision that where all INEDs are long-serving, issuers should appoint a new INED and disclose the length of tenure of all the independents on a named basis. This puts Hong Kong behind Singapore, which introduced a nine-year hard stop on INED tenure. As of 31 August 2023, there were around 1,500 directorships held by long-serving INEDs at 800 listed companies (roughly one-third of all issuers). There are still around 50 listed companies where all the INEDs are long-serving.[1]

It is only a recommendation that INEDS do not receive equity-based compensation

The 2021 CG code overhaul also saw a 'recommended best practice' (RBP) that INEDs should not be given equity-based compensation (we argued at the time that this did not go far enough: issuers are free to ignore RBPs and commonly do.) Again it is worth stressing that secondary issuers in Hong Kong are not required to follow the CG Code: as our listed company research demonstrates, this pulls down the quality of the market.

[1] HKEX Review of Issuers Annual Disclosure on Corporate Governance, 2023

Board chairs can still lead the nomination committee

We bumped Hong Kong up by half a point because it upgraded a CG code provision for a mandatory nomination committee to a listing rule effective 1 January 2022. But it was bittersweet: HKEX backed down on a proposal that the committee be chaired by an INED. Either a board chair or an INED can chair the NC and the majority of members should be INEDs. This was despite significant support for a NC chaired by an INED and comprising a majority of INEDs: in the consultation, 83% of respondents supported the proposal yet the 17% minority got the result they desired.

Issuers need to communicate more with shareholders

HKEX now requires an annual review of companies' shareholder communication policies given increasing investor demand for engagement with issuers. Quite telling was the narrative some listed companies projected when protesting the issue of a shareholder communications policy: "impracticable and unduly burdensome for issuers to allocate expenditure on investor relations staff and infrastructure." Some companies "worried that stakeholder engagement would interfere with how the board manage the company." They argued that "a board should be permitted to manage the company on behalf of shareholders free from interference." Lead INEDs may not be able to be go-betweens because "they may not be familiar with the day-to-day operations of the company." Mercifully the listed companies were in a minority: 89% of respondents supported the proposal.

Stewardship and spinoff guidance leave much to be desired

On the issue of stewardship, Hong Kong lost marks for failing to upgrade its non-binding, voluntary Principles of Responsible Ownership since 2016. Hong Kong is behind the curve. We also docked a point for the listing rules, and in particular waivers, for issuers seeking to spin off the business on a PRC stock exchange. HKEX received consent from the SFC back in 2016 to grant waivers to companies from giving shareholders entitlements in a spin off on a PRC bourse. HKEX's practice note 15 gives an assured entitlement by way of distribution in specie of existing shares, or preferred application in any offering of new shares. The argument is that PRC law technically does not allow non-PRC shareholders to hold domestic shares, hence they could not offer them equity in the spun off entity. The guidance from HKEX's Listing Committee is that companies should get a letter from their legal advisors, as well as board assurance that the spin-off and waiver "are fair and reasonable in the interests of the issuer and its shareholders." Issuers must also disclose details of the waiver.

Companies no longer have to justify having the same chair and CEO

The 2021 consultation also saw HKEX drop a requirement for companies to state whether the role of chairman and chief executive are separate and exercised by different individuals. Obviously it can be easily worked out by checking the names of these individuals but taking away the prominence of this disclosure in companies' annual report was quite telling: issuers no longer are forced to give reasons why they have not separated the two roles. If HKEX requires lead INEDs under the June 2024 consultation, this could again highlight the lack of independent chairs.

Disclosure on share award schemes with caveats

Shareholders are less able to veto share award grants to insiders

A new disclosure regime for share award schemes came into effect on 1 January 2023: previously Chapter 17 of the rules only covered share options. While a regime to cover all awards is beneficial in allowing shareholders to know who gets an equity grant and why, it came with a sting in the tail. The new regime relaxed requirements for shareholder approval of share award grants to connected persons. In the past, any grant of share awards to a connected person would have to be approved by independent shareholders regardless of the size of grant. The new regime introduced a de minimus threshold: approval from independent shareholders is only

required for awards to a connected party, substantial shareholder and controlling shareholder if the grant exceeds 0.1% of issued shares in a 12-month period. But HKEX dropped on a proposal that it would be the remuneration committee, rather than INEDs, who approved all share schemes at an issuer. This role remains with INEDs. HKEX did not take the opportunity to rethink its January 2022 CG code revision that INEDs generally should not be granted equity-based remuneration as a recommended best practice only.

Full-ish steam ahead on ESG reporting

Climate disclosure is set for a revamp

Companies in Hong Kong have been required to issue an ESG report on a comply or explain basis since 2016 and improvements were made to the regime in 2020. In April 2023 HKEX consulted on further changes to the framework which would see mandatory climate reporting (currently companies must only disclose on a comply or explain basis) based on the IFRS S2 standard published by the International Sustainability Standards Board (ISSB). It jumped the gun somewhat, with ISSB not having finalised its own standards by that point. Nor had the Hong Kong Institute of Certified Public Accountants (HKICPA) at that point consulted its members on ISSB. Under HKEX's proposal, issuers would be expected to disclose from January 2024, with interim provisions for Scope 3 and current/anticipated financial effects for the first two reporting years and full compliance by 2026. In November 2023 the Exchange announced that implementation of any listing rule changes would be pushed back to January 2025 "to allow issuers more time to familiarise themselves with the new (ISSB) climate-related disclosure requirements." This is after ISSB announced it would publish an adoption guide on the final IFRS Sustainability Disclosure Standards to help regulators as they seek to align with the new framework, and adopt phasing-in measures.

Companies do not need to respond to a significant vote against directors

Close calls

The nature of corporate ownership in Hong Kong, with a large number of family or state controlling shareholders, means that directors can be voted in despite a majority of independent shareholders voting against. In the 2021 consultation on changes to the CG Code and listing rules, ACGA advocated that companies in this circumstance be required to make a statement explaining why these directors should stay on the board. In particular, similar lines to Principle 4 of the UK Code of Corporate Governance be followed: "when 20% or more of votes have been cast against a board recommendation for a resolution, the company should explain, when announcing voting results, what actions it intends to take to consult shareholders in order to understand the reasons behind the result." The board should also publish an update of shareholder views and action taken six months after the shareholder meeting. Our proposal was not adopted.

4. Listed companies

Hong Kong moves up a place to rank 6th but on a lower score of 53%

Hong Kong gained a place to rank 6th in this category although on a lower score of 53%, a drop of six percentage points from 2020. It remains ahead of Japan and Korea but trails Singapore by two places.

Overseas issuers follow different rules and disclosure is mixed

This was a category where it became apparent that issuers who are given waivers to follow disclosure rules affect the quality of the market as a whole, particularly when it comes to remuneration. A bright spot was found in the composition of nomination committees: a third of the 15 companies we surveyed have appointed

women chairs (although four issuers had no women at all on their boards) which augurs well for enticing more female directors to join in future. But independent chairs are few and far between - just two issuers scored top marks here - and no issuers have opted to have a lead INED.

Where Hong Kong does well

Disclosure gaps are apparent depending on the type of listing

Director and INED remuneration is an area where Hong Kong puts in a decent performance. The market would have earned top marks were it not for the presence of a large China tech firm which receives a waiver as a secondary listing - and only sets out an aggregate figure for overall remuneration, along with share-based awards held by directors and officers. The score was also dragged down by the presence of an H share company which only listed remuneration for two executive directors: the details on the other director, along with two non-executive directors, were left blank. This was presumably because they are paid directly by the parent company (see the China section for more details on these gaps in disclosure) but it was not made explicit. Also worth mentioning is the presence of an H share company which dutifully describes the remuneration in detail, along with the fact that all the executive directors and one INED waived their director fees in 2022. By large, the issuers in our survey steered clear of compensating independent directors by way of stock options, commissions or a percentage of profits. Again, the presence of China tech firms prevented a straight flush here: while the majority of issuers compensated by way of director fee (and a number of directors held personal shares in the issuers), the PRC tech firms included share options in the remuneration bundle.

Some issuers are good at internal audit disclosure

All but one (again, one China tech firm scores a zero here) issuers disclose details of internal audit - the fact that they have a standalone department, and the parameters of their operation, including reporting lines. Exactly how the relationship works ranges from fairly good to very basic.

Nomination committees are halfway there

Nomination committees are independently chaired at 11 of the companies, and while two companies ticked all of our boxes as having all other members serving as INEDs *and* meeting more than twice a year (China Mobile and PICC), the majority keep directors in the mix or meet just once. It was encouraging to see five of the companies appoint female chairs of the nomination committee, and a further five have women directors present on the committee. But still, four issuers had no women at all on their boards.

Where Hong Kong performs averagely

Annual and ESG reports lack detail, and good luck finding the IR contact!

Companies were only marginally better in describing their ESG/sustainability track record during the past year. Board and committee reports, while often long on words, tend to be very short on granular detail. Or they are simply bullet points. Either way, there is a lack of discernible narrative in terms of what the board actually does in a 12-month period. Similarly, these issuers lag on investor relations: finding an actual person to contact with an email or phone address is a challenge. To date, the emails we sent to half a dozen companies asking for the name of the IR contact remain unanswered.

Details on director training could be better

Nor is much gleaned from reading about directors' training: while most issuers provide training for novices and directors, the quality and quantity of content is something of a black box ('attending seminars, reading materials, joining workshops'). It is worth noting that the June 2024 consultation by HKEX on the Listing Rules and CG Code is proposing mandatory training for directors.

Audit committees look good on paper

On paper, audit committees among the issuers surveyed had candidates with credible accounting, auditing or financial prowess, and look to be independently chaired. In reality, six of the 15 issuers had AC chairs who were ex-partners at their current auditors, and there was a former insider (non-executive director) chairing the committee at another. There were also a few ex-solicitors in there. While other members of these ACs had impressive resumes (former chairs of banks, founders of private equity firms and both current and ex-government officials) they may not be the most obvious candidates to challenge the status quo.

Figure 14

Hong Kong listed companies scores, CG Watch 2023

Question		Average score	Range of scores
1.	Does the company's board governance reporting compare favourably against international best practice?	2	1-4
2.	How would you rate the quality of the company's ESG/sustainability reporting?	3	0.5-4.5
3.	Does the company provide comprehensive, timely and quick access to information for investors?	2.5	1-3.5
4.	Does the company undertake annual board evaluations, either internally or using external consultants?	1	0-3.5
5.	Does the company disclose and implement a credible board diversity policy?	1	0-3
6.	Does the company provide induction and/or ongoing training to all directors?	2	0-3
7.	Does the company have an independent chairman and/or a lead or senior independent director?	1.5	0-5
8.	Does the company disclose total remuneration of each member of the board of directors?	4.5	0-5
9.	Are the independent directors paid partly or wholly in stock options or restricted share awards? Do they share in a percentage of company earnings or other commissions in addition to their base fee?	4.5	0-5
10.	Are audit committees (or an equivalent) independently led and competent in financial reporting/ accounting matters?	4.5	3-5
11.	Does the company have an internal audit department that reports to the audit committee?	3	0-5
12.	Does the company provide a detailed explanation of its executive remuneration policies?	2	1-4
13.	Does the company have a nomination committee and is it independently led?	3	1-5
14.	Does the nomination committee have a female chair or at least one female director?	2.5	0-5

Source: ACGA research. Based on 15 large caps from a range of sectors

Where Hong Kong does poorly

Board evaluations and diversity policies are lacking

Board evaluations are lacking. Eight of the 15 firms made no mention of board evaluations at all, while the remaining seven tended to survey their directors internally and conclude either a) nothing, or b) that everyone is awesome. Only two issuers hired external consultants (and in fairness, one did conclude that its committees needed new terms of reference as a result of the evaluation.) Another area where Hong Kong lagged was in respect of board diversity policies which go beyond woolly statements and actually map out targets, timelines and progress. A boilerplate paragraph or two is the norm here and several issuers had not updated their policy in decades. Eight issuers scored zero points for this question, and it was particularly disappointing to see several companies refer to the presence of one female director as reaching their diversity targets.

Independent chairs are virtually non-existent

There were a few independent chairs in name only, typically appointed by government or long-tenured board members. For the main part, controlling shareholders and founders remain stubbornly at the helm. In all, we found just two genuinely independent chairs out of the 15 companies (Hang Seng Bank and MTR Corp) and none of the issuers have adopted the idea of having a lead INED.

The founder of Hong Kong INED group falls foul of regulators

Do as I say, not as I do
It was an eventful 2023 for the founding president of the Hong Kong Independent Non-Executive Director Association (HKiNED), Anthony Fan Ren Da. The man behind the organisation committed to the professional development of INEDs (and help them understand their duties at listed companies) was in December required by the Stock Exchange to undergo 20 hours of training on regulatory and legal topics - including listing rule compliance - as a result of shortcomings in his performance as an INED.

Audit committee members fail to oversee new money lending business at firm

Fan and fellow INED Dr Loke Yu were among six current and former board members at trademark licensing firm Hong Kong Resources Holdings who in December were publicly censured by the Stock Exchange (two other directors received prejudice statements) after a foray into money lending and inadequate internal controls led to HK$86m in unpaid loans and a large hole in the company's accounts. Fan and Dr Yu took the Stock Exchange to court over the decision but a judge ruled against them, noting both were members of the company's audit committee (Dr Yu was chair of the committee) and had failed to meet their primary responsibility to monitor and oversee internal controls.

Fan is an INED at 11 listed firms in Hong Kong

Still, the public censure and training appear not to have dented their popularity as INEDs. Fan currently serves as an INED on 11 boards, while Dr Yu is an independent director at four listed companies.

5. Investors

Hong Kong stays in 9th place with 33%

Hong Kong remained in 9th place in this category with a slightly lower score of 33%: a percentage point was shaved off its 2020 performance when it managed to break the 30% barrier (scoring 34%.) It is behind Singapore which fell one place to rank 7th on a score of 39% and there is a yawning gap between Australia and Japan which are in the mid to late 60s.

Domestic players remain on the sidelines in supporting CG

A familiar story has emerged, that of the domestic-foreign divide in how investors show their support for CG in Hong Kong. The large domestic asset owners reveal little about their CG approach and stewardship practices. Domestic investors remain muted as their foreign peers remain the institutional voice of CG in the city. Even so, the foreign contingent appear less willing to opine on market matters: recent consultations have typically only seen one or two international institutional investors chime in with comments and pushback.

Seen but not heard

Domestic players are keeping their heads down

Most of the big asset owners in town are a black box when it comes to their approach and efforts on corporate governance. The Hospital Authority, Jockey Club and Housing Authority offer no insight, leaving just the Hong Kong Monetary Authority (HKMA) and AIA Group with visible CG policies. Likewise, domestic asset managers stay under the radar on CG.

HKIFA echoes some of ACGA's concerns

ACGA has been pleased to see the Hong Kong Investment Funds Association (HKIFA) shares our concerns over certain CG issues: transparency of directors' details, and more recently the decision by HKEX to scrap separate class rights for holders of H shares. Otherwise, domestic asset owners and managers are reticent in consultations: the H share issue, which proposed upending fundamental rights,

attracted no local voices. Only BlackRock® and an anonymous investment manager spoke up in the consultation from the investor side (although the Hong Kong Investment Funds Association did put in a submission in which it voiced significant alarm.) Generally, investors are not wading into public debate and the investor score reflects this.

Do they vote and engage?

The general mandate is still consistently voted against

Both domestic and international shareholders consistently vote against the general mandate in Hong Kong. While domestic managers are less explicit on their voting, the foreign contingent score top marks here. A similar picture emerges in respect of collective engagement: we know some foreign investors do both individual and collective engagement but at best, domestic investors talk of engagement in general terms. Disclosure is thin on the ground. The only engagement to spill into the public domain in recent years was the lobbying of HSBC in 2022 and 2023 by Ping An, which pushed for the lender to spin off its Asian operations into a separate business. The PRC insurer held just over 8% of HSBC. The standoff led to the formation of the one-man "Spin Off HSBC Asia Concern Group'' which in April 2023 urged shareholders to vote for a restructuring of HSBC's business at its 5 May AGM. They failed to secure the vote, as major institutional investors vetoed the plan.

Touching the void on activism

Activist funds and short sellers pack their bags

Hong Kong lacks an activist fund space given the presence of controlling shareholders and only occasionally are there campaigns of interest. Elliott Management's 10-year battle with Bank of East Asia culminated in the lender repurchasing the shares held by the activist in 2022. The previous year Elliott shuttered its office in Hong Kong. Other activist funds in Hong Kong meanwhile have focussed their efforts on markets such as South Korea and Japan. Similarly there has been a notable decline of short seller action involving Hong Kong listed companies since the decision by the securities regulator to pursue - and successfully secure - a ban on short seller Andrew Left in 2016 for his "reckless" report on PRC property behemoth China Evergrande. Left published the report on China Evergrande in 2012 in which he warned the real estate giant was at risk of insolvency. The rest, as they say, is history.

Retail punters take to social media

Campaigns by retail investors are haphazard

Unlike Singapore, Hong Kong lacks an association or body which caters exclusively to the retail investor base. Webb-site editor David Webb tried back in the day: his proposal for a Hong Kong Association of Minority Shareholders (HAMS) funded by a 0.005% "Good Governance Levy" on market transactions failed to get government support in 2002. The SFC picks up some of the slack with its educational initiatives for retail investors - TV dramas, radio segments and public service announcements - but without a formal vehicle for collective retail action, there simply is not much of note in the way of campaigns against rogue directors and companies. David Webb remains a meticulous watchdog of nefarious corporate deeds but ill health has limited the frequency of his reports.

Occasionally punters do pack a punch

Ad hoc alliances do occasionally spill into the public domain via Facebook and other social media: a 2023 spat between shareholders and the board of local broadcaster TVB saw the two sides square off over profitability, with the former threatening an EGM. The TVB Shareholders Alliance garnered support via Facebook and swiftly hit a nerve with the broadcaster amid salacious allegations. Still, there remains a lack of retail action spilling over into the legal domain thanks to the prohibitive costs and burden: typically, litigious attempts to obtain shareholder recourse are initiated by the SFC (see our chapter on Regulators: Enforcement.)

Listing rule changes have stripped holders of H shares of a separate vote . . .

The great H share stalemate

In August 2023 Hong Kong's stock exchange changed the listing rules to expunge a requirement of separate class votes for holders of H shares where their rights are to be varied or abolished. There would be no separate say, for example, in a share issuance or repurchase. But taking a slightly different view, the SFC still required separate class votes for a privatisation or delisting. Hong Kong Exchanges and Clearing (HKEX) was adamant that the PRC had abolished class distinctions: A and H shares are one of the same, so the listing rules should reflect this. The SFC on the other hand, took the view that although H shares and domestic shares may be as one under PRC law, the fact that they are not directly fungible "warrants a different approach" when applying certain parts of the takeover and share buy-back rules.

. . . but things have not gone quite according to plan

The catch is that H share issuers need to alter their Articles of Association to give effect to this disbandment of separate class votes. And this has to be achieved by putting it to a separate class vote for holders of H shares. H share issuers have not been racing to change their articles, with foreign investors somewhat reticent to vote in favour of a move which will curtail their substantive rights. Most of the H share heavyweights have yet to broach the issue with foreign investors. In May 2023 Zhejiang Expressway dropped article changes in respect of H investor voting rights from its AGM agenda after investors made it clear they would vote against them.

6. Auditors & audit regulators

Hong Kong ranks 6th with a score of 81%

There was no change in Hong Kong's score compared to our last CG Watch, but it dropped to 6th place from 3rd as other markets - notably Taiwan and Japan - surged ahead in the league table in what turned out to be a very tight race. On the one hand, the expansion of powers at the audit oversight body bumped up Hong Kong's score slightly, only for it to be pulled down by the presence of Listing Rule waivers given to issuers on their disclosure of audit and non-audit fees. Otherwise Hong Kong continues to score top marks for accounting and auditing standards, adoption of key audit matters and timely disclosure of the audit regulator's work.

It was a very close race for several markets in this category

It is worth noting that there were just a few percentage points between the markets here. Hong Kong is a credible member of the 80% club, being narrowly pipped by Singapore and Australia who both scored 82%, and Taiwan and Japan who both scored 83%. Malaysia ranks 1st with 92%, the clear standout in the region in terms of audit standards and audit independence.

A disclosure gap on fees

Not all issuers must disclose analysis of audit and non-audit fees

One of the questions we ask in CG Watch is whether there is a requirement that details of audit and non-audit fees paid to an external auditor be disclosed, along with a narrative which makes it sufficiently clear what the non-audit work is. Hong Kong lost a point here as we took a harder line on the effect of secondary listings and the automatic waivers they receive from the listing rules. Hong Kong's CG Code does require mandatory disclosure and analysis of audit and non-audit fees. The analysis in respect of non-audit work must include details of the nature of the services and the fees paid in respect of each significant non-audit service assignment. Secondary listings are waived from following the Code in its entirety.

Candidates standing for HKICPA election need to get approval

Governing the accountants

One development since our last CG Watch has been an overhaul of the way accountants are able to elect their representatives. In a move which appeared to underscore government concerns over the political leanings of the HKICPA ("Some are concerned that the Council election has become increasingly politicised and deviated from professionalism in recent years," said a May 2022 Legislative Council brief by the Financial Services and Treasury Bureau) in 2022 legislation was passed to amend the way Council members are elected at the HKICPA. The Professional Accountants (Amendment) Bill 2022 increased the number of nominations required for a candidate from two to 10. In order to stand for election, candidates also have to be nominated by two members of a government-appointed body: the Advisory Committee to the AFRC. This Advisory Committee advises the AFRC on "matters of policy regarding any of its regulatory objectives and functions," according to legislation, and must meet at least once every three months. It comprises the chair and CEO of the AFRC along with two other AFRC directors (all AFRC members are appointed by Hong Kong's Chief Executive). A further eight to 12 members of the Advisory Committee are appointed by the Financial Secretary.

Auditor oversight body sees its powers expanded

A new name, a new identity

We increased Hong Kong's score due to the work of the audit oversight body, which also has a new website. As we reported in our last CG Watch, 2019 was a game changer for Hong Kong as it ushered in a fully-fledged independent audit regulator. Since then the Financial Reporting Council (FRC) as it then was has rebranded to become the Accounting and Financial Reporting Council (AFRC). The body in 2019 took over the inspection and disciplinary powers of the Hong Kong Institute of Certified Public Accountants (HKICPA), leaving the Institute with registration, education and standard setting. In 2021, the FRC became the AFRC and in October 2022 saw its statutory function expanded to include everything but standard-setting. Its broadened remit also included oversight of the performance of the HKICPA.

CPAs are flunking CPD compliance

Keeping tabs on the profession

The past two reports issued by the AFRC on their oversight role of the HKICPA leaves no doubt that they take the role seriously: the November 2023 oversight report on the Institute's functions made for painful reading in parts. Adherence to continuing professional development (CPD) requirements in particular turned out to be particularly sticky, with nearly one in three CPAs surveyed failing to comply (triple the rate of the previous year). In July 2023 the AFRC came out with a chunky 94-page report on its inspections during the three-year period up to the end of 2022, by which time it had inspected all six Category A firms[2] once in each year, and each Category B and C firms at least once during the three-year cycle. Category A firms dominate the market for listed entity audits and are inspected annually.

Audit quality scrutiny yields mixed results

The inspection report notes that four of the six Category A firms were more proactive than the remaining two in responding to the AFRC's findings and improving the quality of their audits. Indeed, there were "recurring deficiencies" in the other two. Nor was there much improvement over the three years in the inspection results of the Category B and C firms, leading the AFRC to conclude that the state of play is "unacceptable and disappointing."

[2] Category A firms are those with more than 100 Public Interest Entity (PIE) audit clients, B firms have 10 to 100 PIE audit clients, and C firms have less than 10. PIE refers to public interest entities (ie, a listed corporation or collective investment scheme.) There are currently 78 PIE auditors in Hong Kong.

The bigger firms do better in general

Among the leading six, scores on the average audit quality are improving. Deloitte and EY lead the pack with a rating of 2 in 2022 (the lower the score, the better) followed closely by KPMG and PWC who earned a 2.2 and 2.3 respectively. Meanwhile BDO and HLB Hodgson Impey Cheng (HLB) lag their peers by quite a wide margin, with ratings of 3.2 and 3 respectively. Category B firms score an overall 3.4. Still, it is worth noting that a few of the Big Four firms were being given ratings in the region of 3 or more back in 2020. The message which permeates the findings is that the Big Four appear to be taking the process more seriously than others. Across the board, AFRC identifies where the audit quality deficiencies are, and where they are growing. Of note is the increase in problems with group audits and in particular insufficient direction and supervision by lead auditors and shortcomings in how group engagement teams document evaluations of component auditors. The use of auditor's experts was also flagged, particularly amid the Covid backdrop and an increased use of outside specialists to help with impairment factors. On the upside, there was an improvement in the exercise of professional scepticism.

When the going gets tough . . .

Eleventh hour resignations by auditors attract scorn

Another focus area of the AFRC is quality control, and there has been one particular area which has drawn ire from the regulator: late auditor resignations. A surge in last-minute exits (ie, less than a month before, or after, the end of the reporting period) prompted two open letters from the AFRC in October 2022 and January 2023. Statistics revealed that late resignations jumped to 107 in 2022 compared to 71 in 2021. In nearly two thirds of cases, the catch-all 'inability to agree on auditors' fee' was cited, while 30% quit amid unresolved audit issues. Concern was raised by the AFRC that the incoming auditors were short on requisite competence and capacity to perform the audit within a limited time frame. There was an improvement by the time the AFRC penned its second letter in January 2023 - the rate of late resignations had decreased - but still it took aim at an apparent pivot by issuers to using voluntary rotation as a means to abruptly change auditors, as well as opinion shopping.

Stick or twist?

Who is moving away from the Big Four? The AFRC's 2023 inspection report noted that some Category B and C firms are taking on more listed entity audits with larger market capitalisations: as figures stand, nearly a third of all appointments are with these smaller outfits.

Category B firms have a notable slice of audits

Figure 15

Market share of listed entity audits

	Firm	Number of appointments	% of appointments	% of market cap
1.	PWC	440	17.2	44.1
2.	EY	388	15.1	18.1
3.	Deloitte	277	10.8	17.0
4.	KPMG	229	8.9	10.0
5.	BDO	213	8.3	0.7
6.	HLB	125	4.9	0.4
7.	Category B	694	27.1	3.1
8.	Category C	64	2.5	0.1
Recognized firms[3]				
9.	Mainland China	86	3.4	1.3
10.	Overseas	47	1.8	5.2

Source: AFRC 2022 Inspection Report

[3] There are 11 mainland firms under a mutual recognition agreement who audit PRC companies listed in Hong Kong and 25 overseas firms. Many of the latter are network firms of Category A firms. AFRC did not select any firms for inspection from these categories, citing their relatively small share of listed entity audits.

Since the 2021 inspection report, the number of Category B firms has increased by 4 to 19, and the category C firms have declined, as there were 23 in 2021 and 19 in 2022. Category B firms in 2021 accounted for 582 listed companies audited, with market cap of 2.2%. In 2023, the figure had risen to 694 auditor appointments.

No blockbusters yet

A lot more complaints are being pursued

The AFRC's expanded role has unsurprisingly seen its workload proliferate: the investigation and compliance department saw an 83% increase in pursuable complaints (there were 253 processed, resulting in 60 investigations) according to its September 2023 Investigation and Compliance report, and the number of financial statements it proactively reviewed went up by 73% to 130, although only 8 resulted in an investigation. The transitioning role of the AFRC meant that it was only in October 2019 that the body (then the FRC) became fully responsible to scrutinize irregularities in financial statements (the task having previously been with the HKICPA), so its focus will have been on audits after that date.

Most complaints to the AFRC come from the general public

Still, behind the figure of an 83% year-on-year increase in pursuable complaints received, the number of complaints closed grew even more: this figure increased to 122. The AFRC cites the lack of clear and concise information and supporting evidence. Complaints involving PIE audits numbered 114 in 2023, and interestingly the vast majority (59%) came from members of the public. Just 3% of complaints came from the SFC and 9% from the Stock Exchange. The remaining 29% resulted from AFRC inspections. Nearly half of the complaints related to audit quality issues, while 23% were due to issues with independence, integrity and other professional misconduct. In terms of the type of firm at the heart of these complaints, category A audit firms accounted for 44% of complaints, with Category B and C firms accounting for 40% and 16% respectively.

There have been a few reprimands and fines

During 2023 there were 60 new investigations of PIE auditors compared to 32 the previous year. Of the 142 cases handled during the year, just three were completed So the running total appears to be that there are 139 cases in progress. The investigation report gives much insight into general problems which seem to arise from these complaints but few appear to attract big ticket sanctions. PIE auditors are liable to a financial penalty of up to HK$10m or three times the profit or loss caused by misconduct, whichever is higher. The most severe penalty in 2023 appears to be the decision in November to permanently revoke the practising certificate of sole proprietor Chan Kam Kwan and fine him HK$300,000 (US$38,400) after he was found to have "blindly signed off" on 11 auditor reports of private companies. There was also the August 2023 reprimand of a local CPA firm, ZD CPA, its engagement partner Chan Kam Fuk and engagement quality control reviewer Ling Chun Kwok, who in total received a HK$700,000 penalty. The practising certificate of Mr Chan was also cancelled for 12 months for breaches relating to the audit of Hong Kong-listed China Infrastructure Investment and its subsidiaries for the 2016 financial year. The third disciplinary case in 2023 resulted from a failure to rectify shortcomings following an AFRC inspection, which resulted in a HK$80,000 fine (US$10,200).

7. Civil society & media

Hong Kong falls to 7th place on a score of 50%

Hong Kong fell one place to rank 7th in this category but on a much lower score of 50%, a ten percentage point drop from 2020. It has been overtaken by Malaysia, which moved up two places to 6th with a score of 53. Singapore is now a good 14 percentage points ahead of Hong Kong, scoring 64%, while Australia is well ahead with 82%.

Upskilling offerings remain solid

Director training is a bright spot

There was a bump in score for director and company secretary training on corporate governance, with the Hong Kong Institute of Directors offering a variety of topics and speakers as part of its professional development agenda. This included certificate courses on the role of a company director, finance for directors and on how ESG creates value for companies. The Chartered Governance Institute of Hong Kong (formerly known as the Institute of Chartered Secretaries), now in its 75th year, has a strong CG focus in its professional development courses as well as its signature Annual Corporate and Regulatory Update. The CFA Society (formerly the Hong Kong Society of Financial Analysts) also offers a mix of continuing professional development and career training which does touch on CG issues.

The professionals and business groups tread water . . .

Professions and business groups tend to look at CG through a narrow lens

It has been a longstanding frustration of ACGA over the years that professional and business groups talk about CG topics in their professional development programmes and stay on top of key developments, but do not take a compelling CG advocacy position. This is particularly so with consultations where responses tend to be wholly micro without any consideration of the bigger CG picture. The Law Society takes a narrow, technical view on governance-related consultations and the Bar Association simply no longer responds. An exception here is the Hong Kong Institute of Certified Public Accountants (HKICPA) which does highlight wider CG shortcomings in its submissions.

The pro-issuer lobby is true to form

The Chamber of Hong Kong Listed Companies takes a strong view on anything to do with market development and has become a major voice as others have tapered off. But its agenda is unequivocally pro-issuer. It was opposed to HKEX's proposal in 2021 for an independent vote on long-tenured INEDs (see our section on CG Rules) and took a position against single gender boards on listed companies by 2025: "To say a single gender board is not diversified is to negate an issuers' efforts in achieving other aspects of diversity, which are equally important."

. . . as the investment industry sticks to its guns

Investor bodies are fighting the CG corner on issues close to their hearts

There has been pushback by the investment industry on several market developments which ACGA also advocated against: public access to directors' details at the Companies Registry, and the decision by HKEX in 2023 to change the listing rules on separate class votes for holders of H shares. The Asia Securities Industry & Financial Markets Association (ASIFMA) shared ACGA's view that the repeal of such class meetings would erode protections available to these shareholders, and that long term it would reduce the size and liquidity of the H share market. The Hong Kong Investment Funds Association (HKIFA) took a similar view, and challenged the lack of proper consultation on HKEX's decision: "We are deeply concerned that such a fundamental change can be brought to the market in such an understated manner."

Academics are silent on CG

Academic research shrinks

We scoured academic research in the past few years for any key developments which have taken place in the capital markets, and the CG ramifications, in vain. There was no academic take of note on weighted voting rights, SPACs, Stock Connect, listed companies in general and market reforms in particular from an established Hong Kong academic institution. Overseas academics - in China, Singapore, India, the US - do broach some of these topics from afar, usually as a multi-market comparison. According to press reports[4], 361 academics left Hong Kong's universities in 2022 (there are eight), a turnover rate of 7.4%. Quoted in the Financial Times, Carsten Holz, professor of economics and the Hong Kong University of Science and Technology, said the "critically thinking researchers have left," and universities were hiring juniors who undertake "apolitical research . . . that they know is politically acceptable."

Fears of breaching security laws are prevalent

This comes against the backdrop not only of the Beijing-imposed National Security Law introduced in July 2020 but Article 23 legislation, Hong Kong's separate law on national security which it was required to enact under the Basic Law. The two laws sit aside each other. A concern among academics (and business groups and journalists) is the scope of 'state secrets' and what would amount to unlawful disclosure. According to the Article 23 law, state secrets could include major policy decisions, scientific technology, and information about the city's economic, social and technological developments. It would also be an offence to incite disaffection, which includes bringing 'hatred or contempt' against PRC and Hong Kong government officials, as well as legislators and judges.

In the line of fire

News outlets are forced to close and press freedom has sunk

Hong Kong's press has been hollowed out over the past few years. News outlets have been forced to close and Hong Kong is currently in 140th place in Reporters Sans Frontiers' World Press Freedom index, just a few places ahead of the UAE and behind the Philippines, Singapore, Indonesia and Thailand. In 2018, it was in 70th place. According to RSF, 11 journalists and one media worker in Hong Kong are currently in detention.

Apple Daily publisher Jimmy Lai is on trial for NSL violations

The industry lost a major player in 2021, with the forced closure of Jimmy Lai's flagship Apple Daily. The popular pro-democracy tabloid was raided by police in August 2020 two months after the National Security Law (NSL) was passed and in June 2021 its assets, and those of Jimmy Lai, were frozen by the authorities. As we write, 76-year-old Lai is currently on trial at the High Court in Hong Kong for violations of the NSL including sedition and collusion with foreign forces. He faces life imprisonment.

News groups tread a cautious line

What is left are politically neutral local news groups, the pro-Beijing contingent in the city, and the foreign press. But work visas can be a nail-biting issue for the latter: in July 2020, New York Times journalist Chris Buckley was denied a visa, and the same happened to a Hong Kong Free Press writer in August 2020. The Economist journalist Sue-Lin Wong, host of the "Prince" 12-part podcast on the life of Chinese president Xi Jinping, did not have her Hong Kong work permit renewed in November 2021.

[4] Financial Times, 24 October 2023

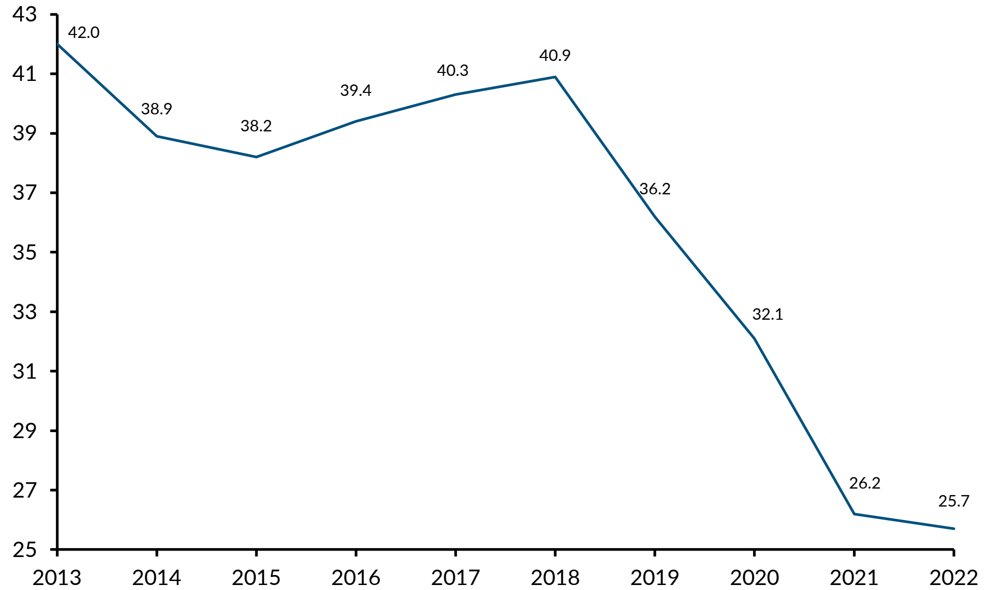
Journalists worry about criticising the government

The media in Hong Kong believe Hong Kong "no longer has space for critical voices," according to the industry's de facto trade union, the Hong Kong Journalists Association (HKJA), and this has led to less access to information for the general public. Hesitation in criticising the central government was the main reason behind a further decline of press freedom in 2022, according to the association.

The media in Hong Kong are not optimistic about press freedom

Figure 16

Journalists' rating on press freedom in Hong Kong, 2013-2022



Source: Hong Kong Journalists Association

The journalist union is subjected to a tax review

The 55-year-old HKJA has seen its membership fall from around 800 in 2019 to 300. In January 2024 it announced that the Inland Revenue Department (IRD) had requested detailed accounting records for several years, as well as tax returns for the six years up to 2022. The IRD subsequently informed it that the organisation's taxes had been reviewed, and that it was liable for HK$400,000 based on the size of the HKJA's bank deposits. "We were perplexed by this," the organisation wrote. Its operational funding is derived from sponsorship at its annual dinners. The HKJA is also the subject of an investigation by the Registry of Trade Unions, the government body which regulates unions, which in January 2022 asked for financial data and information on past events. In April 2022 the press group held an EGM to discuss the future of the group, including whether it should disband.

Bad corporate behaviour is less likely to be reported

The reduced scale and scope of the press in Hong Kong has seen exposes on corporate and director abuses greatly diminished. Original investigative work is rare.

A reporter accesses license plate data as part of a documentary

A journalist lands in the dock for a public record search
A core feature of any journalist's job is to search public records for information. Reporter and television producer Bao Choy did just this when she sought to find out who was behind an attack by an organised crime mob on commuters returning home from work in July 2019. A group of men in white t-shirts let rip with steel rods and canes on pedestrians and people boarding a train at Yuen Long MTR station. The attack was during the height of the 2019 protests and police arrived nearly 40 minutes after the incident, notwithstanding 24,000 calls to emergency services. The RTHK journalist, working on a documentary on the attack, searched vehicle registration records to identify suspects. In particular, there was one car which was used to transport some of the mob and deliver weapons to them.

She is convicted for ticking a box when making the search

She was arrested in November 2020 and convicted in April 2021, of knowingly making a false statement when she conducted the search: the box she had ticked from a pulldown menu on the Department of Transport website, 'other traffic and transport related matters,' was false, prosecutors argued. Her real reason for applying for the certificate was for investigative journalism, which had no connection with the purpose of road traffic legislation. The journalist was fined HK$3,000.

The journalist takes the case to the top court and wins

The case went all the way to the Court of Final Appeal. In June 2023 it ruled in favour of the journalist, saying a "substantial and grave injustice was done to her," in what was widely seen as a litmus test for the legal parameters of journalistic rights.

Downgrade watchlist

What to avoid

Factors that could force the market score to fall in 2025:

- ❑ No improvement in minority shareholder protections
- ❑ Any significant changes to Hong Kong's anti-corruption and financial crime agendas, and any additional moves to restrict public access to directors' and corporate information.
- ❑ A disappointing outcome on proposed changes to the CG Code and Listing Rules in the June 2024 consultation by HKEX which could see lead INEDs, a cap on INED tenure at nine years and the appointment of female directors to the nomination committee, among other things.
- ❑ A formal registration system for the media, internet and information control, and political prosecutions of journalists. Further evidence of a diminished academic presence.

Next Steps

Our recommendations for the next stage of CG reform in Hong Kong include the following:

End the practice of 200-page consultations with predetermined outcomes

1. **Public consultations:** investors may be more inclined to make submissions if consultations are shorter, ask open-ended questions which stimulate objective opinions and take greater account of investor feedback, particularly where associations and industry bodies are responding on behalf of members.

Level the playing field for investors seeking recourse

2. **Take action on class actions and alternative fee structures**: Hong Kong has failed to introduce a class action regime despite previous commitments to do so.

Review the work and outcomes of the MMT

3. **A review of the Market Misconduct Tribunal**: a deep dive into the processes, hurdles and outcomes of the MMT would be interesting. Identify areas where the process can be streamlined, determine why cases take so long to complete, and map out a leaner, quicker resolution process.

Revise the stewardship code

4. **Revise the stewardship code**: an overhaul could invigorate the stewardship space.

Investors would like to see tighter CG rules

5. **CG rules**: move ahead with planned changes to the CG Code and Listing Rules in the June 2024 HKEX consultation, including limiting INED tenure, overboarding and introducing lead INEDs. Investors have been waiting for these changes.

Take a hard line on auditors who use fee disagreement as excuse to resign

6. **Auditors**: regulators could banish the use of the 'disagreement over audit fees' catchall excuse as a reason for parting ways with auditors so close to financial results. Regulators could be more robust in pursuing auditors who suddenly resign and it then transpires that there are significant problems with the financials.

Company checklist

Actions companies could take to enhance CG practice and disclosure immediately

Actions companies could take over the short to medium term to enhance their governance practices and disclosure include the following:

1. **Provide investor relations contacts**: a name, phone number, and email address would make it easier for investors to find out information about a company and connect with the IR team.

2. **Composition/structure**: boards could go beyond the obvious networks to seek new candidates, limit INED tenure and curtail overboarding. Nomination committees chaired by INEDs would be a welcome standard practice, even if it does not appear in the HKEX consultation on the CG Code and Listing Rules published in June 2024.

3. **Board reporting**: granular details on how the board operates, the decisions it takes in a given year and the process of coming to these would be welcome. Committee reports could go beyond simply setting out terms of reference and what is reviewed on an annual basis. Bios should go beyond education, career experience and other affiliations and provide insight into why this particular candidate is suitable for the job.

4. **Gender diversity**: issuers chould set out in detail the steps they are taking to attract more women to the board, how the pipeline is shaping up and what progress is being made. Targets and timelines should be set out, along with progress reports. Appoint a woman to chair the nomination committee.

5. **Board evaluations**: companies could go beyond an annual questionnaire and appoint a third party to scrutinize the performance of directors. Make it explicit to shareholders what the results of the external evaluation are, and report on any areas where directors have fallen short and what remedial action is being taken.

Jamie Allen
Former Secretary General, ACGA

Lake Wang
Research Manager, ACGA
lake@acga-asia.org
+852 2160 1785

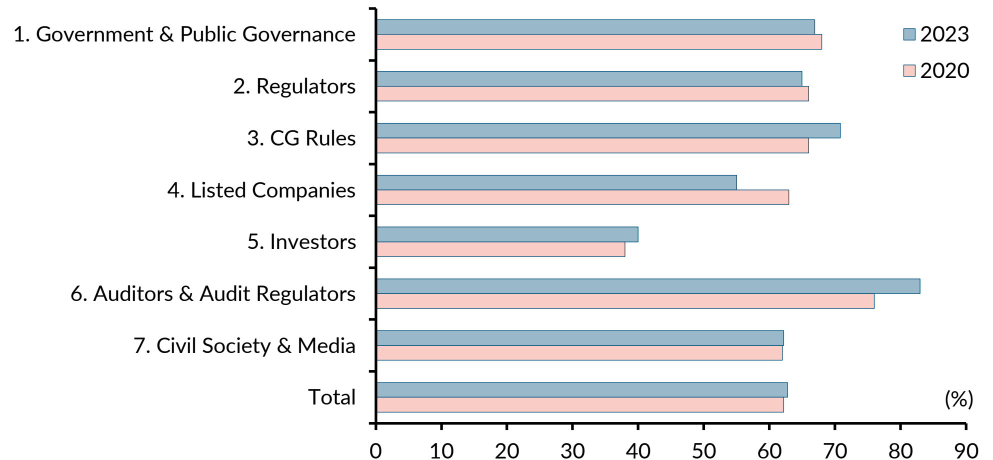
Acknowledgement
Neesha Wolf, Former Taiwan Research Director, ACGA, contributed to the research and scoring of this chapter.

Taiwan - Holding its own and improving

- Taiwan's overall market score rose 0.6 percentage points and it improved one place in ranking to equal 3rd with Singapore. Most category scores strengthened or held steady, but CG disclosure remains superficial
- Major focus on sustainability with a Sustainable Development Guidemap for listed companies in 2022 and Action Plan in 2023. Taiwan ahead of most of the region in mandating some level of assurance for sustainability reports
- A new Audit Quality Indicator (AQI) framework and transparency reporting for audit firms
- A new Commercial Court in 2021 is a gamechanger and unusual for the region
- Outdated rules amended on substantial disclosure (now 5%), blackout periods for director trading, and enhanced director remuneration disclosure
- Problematic regulations remain: related-party transactions, virtual AGMs, and legal-entity directors
- Investor stewardship broadening and deepening, with investors encouraged to disclose voting down to the company and resolution level and improved disclosure of stewardship policies and activities
- An increasingly vibrant civil society and director training ecosystem

Click to rate this research

Figure 17
Taiwan CG macro category scores: 2023 vs 2020



Source: ACGA

Taiwan rises in three categories, holds steady in three, falls in one

Introduction

Taiwan's approach to CG reform has been broadly consistent for the past 10 years

Taiwan's approach to CG reform has long been top-down, driven by government, a strategy that brings many advantages as well as some shortcomings. It was not the first market to start modernising its governance regime in the early 2000s, but it remains one of the most consistent in policy terms over the past 10 or more years. It was also not the first market to develop a coherent national strategy for corporate governance, but since its inaugural CG roadmap was released in 2013 it has updated and refined its plans on a regular basis. Taiwan's commitment to reform is made possible by a highly integrated administrative environment (units of government work closely together) and outward-looking regulatory leadership. It cares about its international reputation and takes careful note of developments both regionally and globally. This mindset underscores its overall rise in our rankings from 6th in 2012 and 2014 to 4th in 2016 and 2020, and now equal 3rd. (It briefly dipped to 5th in 2018.)

Taiwan phases in reforms for large, medium, and small issuers

Part of the foundation of this consistency has been a determinedly focussed and phased approach to reform, which introduces new best practices in board governance and disclosure first for large listed companies, followed by mid-sized and later small firms. For example, the Securities and Exchange Act (SEA), Taiwan's main securities law, was first amended in 2006 to introduce independent directors and audit committees, yet it was not until 2017 that all listed companies were required to appoint them and 2022 when audit committees became mandatory for smaller issuers. Such a framework signals clearly to corporates what is coming and minimises surprises.

There are limitations to Taiwan's top-down approach, in particular hastily devised rules without sufficient consultation

The limitations to this strategy are perhaps predictable. In light of Taiwan's post-1949 history of authoritarian leadership and a government-business relationship that remains strongly hierarchical, it is not too surprising that companies tend to do what they are told and rarely push back against government policies with the vehemence found in most other markets in the region. While this cooperative response is refreshing compared to the often negative reaction of businesses elsewhere to demands that they become more transparent and accountable, the risk in Taiwan is that it can lead to policies that have been hastily devised and without adequate consultation. There is a sense that the government is sometimes in too much of a hurry to introduce a reform, whereas it may be healthy for corporates to have more input. The other risk is that companies then just box-tick and do the minimum required, a phenomenon that was apparent in our Listed Companies survey and the reason why Taiwan's category score fell sharply.

Sustainability reporting in Taiwan has emerged from the box-ticking swamp to something more useful

To be fair to Taiwan, corporate box-ticking is alive and well everywhere. Indeed, it is the standard first step in any new form of disclosure, in part because companies rely on consultants to write their reports. One hopes that after a few years the substance emerges. Such is the case in Taiwan with regard to sustainability reporting, which initially was superficial but over time has become considerably more sophisticated. We hope that companies would show the same enthusiasm and commitment to basic CG reporting.

Still many areas where further CG reform is needed

As Taiwan's overall score of 63% shows, CG reform is far from finished in this market. Real progress has been made, but there are still unique aspects to the system that impede good governance such as legal-entity directors, a constrained role for nomination committees, and a fragmented approach to governing related-party transactions (RPTs). We believe the reform momentum will continue.

Recapping CG Watch 2020

Good progress on recommendations from our previous survey

In line with their consistent approach to reform, Taiwan authorities seek to fill gaps in their regulatory regime on an ongoing basis. As the following table shows, significant or partial progress has been made in nine out of 10 areas where ACGA made recommendations in our 2020 survey. While the table does not include all recommendations made, it does reflect many of the more important ones.

Taiwan has made progress on almost all our 2020 recommendations

Figure 18

Taiwan: recap of 2020 recommendations

	Recommendations	Outcomes
1.	Set substantial ownership threshold at 5%	Progress. New regulation cut the threshold from 10% to 5% in May 2023.
2.	Allow virtual AGMs	Partial progress. New regulation issued in March 2022. But aspects of the new rules need to be revised (eg, prohibiting voting on directors and supervisors at virtual meetings).
3.	Boards should become climate ready	In progress. Sustainable Development Roadmap + recommendation for sustainability committees.
4.	More emphasis on company culture in the CG Roadmap and Best Practice Principles, more meaningful CG narrative disclosure	Limited progress. Annual reports still contain a lot of boilerplate CG disclosure.
5.	FSC leadership should have more stability	Progress. Huang Tien-mu was FSC chairman from May 2020 to May 2024.
6.	Improve official online archive of all CG/ESG laws and regulations	Good progress. TWSE website has a Rules and Regulations Directory, while the official online law database is more user-friendly. Organisation of regulations on TWSE website still somewhat random in areas.
7.	Create official website for all CG-related enforcement actions, including updates on outcomes of criminal prosecutions	Partial progress. Detailed Law Enforcement Report published since 2019, yet still hard to find outcomes of criminal prosecutions.
8.	Dispense with legal-entity directors	No progress.
9.	Institutional investors should disclose voting down to the company and resolution level	Partial progress. Investors are now encouraged to do so, and many do.
10	Improve narrative in SFB Audit Oversight Report	Progress. AOB report much improved.

Source: ACGA

1. Government & public governance

Taiwan dropped to 2nd on a marginally reduced score of 67%

Taiwan fell one percentage point in score to 67% for Government & Public Governance and slipped to 2nd place after Australia, having shared top honours with it in 2020. Australia improved three percentage points this time, reaching 71%. Rankings of other top markets also moved, notably Hong Kong which fell from 3rd to 5th after suffering a dramatic drop in score, and Japan which rose from equal 4th to 3rd on a slight increase in score. Singapore remained 4th on a somewhat lower score.

A slightly lower score for national CG strategy

While Taiwan remains focussed on CG reform and is strengthening its policies around sustainable development, sustainability reporting and governance, we slightly reduced the score for our first question on CG strategy to take note of some overly hasty rule changes (eg, virtual AGMs) and only partial progress in key areas such as RPTs (*see CG Rules below for more detail*). Nor has Taiwan been able to resolve certain deeply entrenched obstacles to good governance such as legal-entity directors. These are directors nominated by a legal-person shareholder, namely a corporation, rather than the board itself. Undemocratically, they can be replaced mid-term by the corporate shareholder and without the need for a new shareholder vote in an EGM. This potentially creates problems for board composition and cohesion.

A lower score too for independence of regulators

We also reduced the score for the independence of the FSC from government. The commission board is entirely made up of career civil servants and senior ministers, hence by definition is not independent. Although in practical terms this relationship has been balanced by broadly progressive government policies towards the capital markets over the past 10 years and cross-party support for CG reform, there is a

possibility that this may not always be the case. Relative to other leading markets, where greater policy and operational independence is part of the system, we felt a lower score was appropriate.

Where scores increased

Scores increased on three questions. One related to the governance of banks, where we added half a point for enhanced disclosure around climate risk. Another was on the independence and powers of anti-corruption agencies, which we re-rated upwards largely due to the work of the Ministry of Justice Investigation Bureau (MJIB) and its coordination with other arms of government. The third question related to the effectiveness of anti-corruption efforts in Taiwan, where the score increased slightly on gradually improving trends.

Merging governance and sustainability

Taiwan was ahead of the curve on linking sustainability and financial performance in 2020

Taiwan is moving ahead quickly - and generally faster than other Asian jurisdictions - in linking corporate governance and sustainability. The third version of its national CG roadmap, called "Corporate Governance 3.0 - Sustainable Development Roadmap (2021-2023)", published in September 2020, took some initial steps towards this goal by emphasising the importance of sustainability/ESG reporting and communication with a company's broader group of stakeholders. The Roadmap contained five action plans, the second of which provided some high-level commentary on "ESG information disclosure" and made references to TCFD, SASB, third-party verification of data, and the need for more English-language disclosure. It envisaged expanding the scope of mandatory sustainability reporting in Taiwan and, interestingly, stressed the need to study the "disclosure of financially significant ESG-related information useful for informed investment decision making". Few Asian regulators were talking much about the relevance of sustainability issues to financial performance - a core feature of the SASB standards and central to the new ISSB standards - in late 2020.

Sustainability governance still a new area in 2020

As we noted in CG Watch 2020, however, the approach in "Corporate Governance 3.0" was somewhat tentative from the perspective of "sustainability governance". This refers to the way in which companies should restructure their internal governance mechanisms, including the board, to ensure they meet the new challenges of ESG and climate change. Much of the guidance in the third Roadmap was instead related to board governance in more general terms, in line with previous versions of the document. Another policy statement released around the same time, the Green Finance Action Plan 2.0, emphasised the need for market mechanisms and shareholder activism to drive corporate responses to sustainability and climate change.

Policy ramped up in 2021 and 2022 on net zero and green finance

Things ramped up in April 2021 as the government outlined its intention to achieve net zero by 2050, followed a year later by the publication of 12 key strategies for achieving this goal. One related to green finance, leading to a third version of the Green Finance Action Plan being produced for the finance industry in September 2022. This noted the many areas where Taiwan fell short, such as a workable and sufficiently detailed taxonomy for defining "green" and "sustainable" activities, the need for government agencies to work together to produce consistent and comparable climate and ESG data for financial institutions to access, and the lack of an adequate inventory of Scope 1 and 2 and especially Scope 3 emissions. The new Action Plan laid down broad next steps for these and many other areas. One immediate action was the formation of a collaborative alliance of major financial holding companies, called the "Coalition of Movers and Shakers on Sustainable Finance", whose members committed to such things as green procurement, assurance of ESG information, and joining SBTi.

Next came practical guidance for listed companies

For listed companies, the government produced a "Sustainable Development Guidemap" in March 2022 followed by a related "Sustainable Development Action Plan" a year later. The plan contains five "dimensions", which are both comprehensive and quite bold in parts. A centrepiece is the assurance of GHG emissions data, with deadlines for Scope 1 and 2 emissions - a policy that is ahead of other markets and complements Taiwan's existing requirements for assurance of certain types of ESG data for selected industries. Scope 3 is not mandatory, but companies will be encouraged to disclose these emissions. Regulators are also promoting ideas such as sustainability committees on boards, widening the scope of mandatory sustainability reporting (including the TCFD framework and SASB metrics), emphasising the need for better communication between companies and their shareholders/stakeholders, and creating a standardised ESG disclosure database of company information. While all of these efforts remain a work in progress, they certainly represent more integrated thinking than in the past. Taiwan is trying to develop sustainability policy in a strategic, rather than piecemeal or reactive, manner.

The new Commercial Court

Taiwan is one of the few markets in Asia with a specialised company court

Another initiative that sets Taiwan apart - and one of the more exciting public governance developments in recent years - is a new Intellectual Property and Commercial Court (referred to below as the "Commercial Court"). Established in July 2021 by the Commercial Case Adjudication Act, a key goal is to develop a cadre of judges with specialist expertise who can adjudicate company and securities law cases more efficiently and consistently. One of the issues with the traditional judicial system, for example, is that there are 28 venues (six high courts and 22 district courts) for civil commercial cases under the Supreme Court and judgements between them can be inconsistent - an outcome that has posed challenges over the years for the Securities and Futures Investors Protection Center (SFIPC), which represents small shareholders in mediation, arbitration, and class action lawsuits.

The SFIPC gained access to the Commercial Court in May 2022

The SFIPC gained the right to file civil cases in the Commercial Court in May 2022 and has already seen some significant efficiency gains. Not only has its litigation process been streamlined, it has also enjoyed a notable reduction in the time taken to reach judgements compared to regular courts in the past.

A recent class action case took one third the normal time

In regular courts a typical class action case would previously take an average of 4.2 years, whereas the SFIPC's 2023 case in the new Commercial Court was completed in just over 1.34 years, as Figure 19 shows. The case related to insider trading related to a 2015 hostile takeover of Silicon Precisionware Industries (SPIL) by Advanced Semiconductor Engineering (ASE). While the defendant, ASE's chief operating officer, Dr Tien Wu, was found not guilty by the criminal court, the SFIPC won a partial judgement in the Commercial Court and a payment of NT$48m (US$1.49m), which may go to investors. In March 2024, however, the Supreme Court reversed and remanded the case back to the Commercial Court.

Verdicts in discharge cases have typically taken half the time of regular courts

A similar pattern can be seen in "discharge" suits, where directors or supervisors of listed companies are dismissed from their positions in public companies. These cases typically took an average of 1.5 years in regular courts and sometimes more than five years (see Figure 19). In the Commercial Court, however, the average time has been reduced by half and the longest case has been 1.2 years. One caveat regarding these impressive figures: the number of SFIPC cases in the Commercial Court is still small and it has received discharge verdicts in only eight cases so far.

Court judgements have sped up

Figure 19

New court speeds up judgements in Taiwan, 2019- 31 July 2023		
Regular courts	**Average (No. of years)**	**Range (No. of years)**
Class-action suits	4.23	0.07 to 13.55
Derivative suits	3.87	0.81 to 8.12
Discharge suits (directors)	1.53	0.27 to 5.16
Commercial court		
Class-action suit[1]	1.34	1.13 to 1.55
Discharge suits[1]	0.77	0.53 to 1.19

[1] The limited number of cases in the Commercial Court means that some data is not available. As of July 2023, it had heard 35 cases and given 10 judgements. Only two were class action cases. Source: SFIPC

The expertise of judges has been a critical factor in the new court's efficiency

A key factor driving this efficiency is that many of the judges in the new court have backgrounds in accounting and finance. If they lack expertise in complex areas like merger and acquisition valuations, associate judges with specific expertise will be appointed to write business reports that explain the details to them. These reports will also be sent to the SFIPC, if it is involved in the case, and defendants. Each judge has two business investigators and an assistant to help, while Taiwan Stock Exchange (TWSE) staff have also been embedded in the organisation to support the judges.

Anti-corruption: Gradual progress

Taiwan is rating better in global corruption surveys

The numbers are moving in the right direction for Taiwan in the two most influential surveys of corruption in the region. The most influential global survey, the Corruption Perceptions Index (CPI) from Transparency International, has its score hovering around 61 out of 100 for most of the five years to 2016, then steadily moving up to 68 in 2021 and 2022 before dipping slightly to 67 in 2023. As a result, Taiwan's ranking moved up from 31st out of 180 jurisdictions in the mid-2010s to 25th by the early 2020s. It now stands at 28th.

The same trend is seen in regional corruption surveys

The most widely cited regional survey, published by the Political & Economic Risk Consultancy (PERC), also reports an improving trend. With scores from 0 to 10, with 0 being the best and 10 the worst, Taiwan has remained between 5 to 6 for most of the past 12 years. It hit a low of 6.08 in 2016 and now stands at 4.65. It ranks 6th out of 16 jurisdictions covered.

PERC argues that systemic corruption has been reduced in Taiwan, but warns that political rivalry remains a threat

As PERC said about Taiwan in its March 2024 report:

"Taiwan and South Korea are examples of places where the evolution from more authoritarian political systems to multi-party democracies has been accompanied by reforms that have significantly reduced systemic corruption. Controversial links between business and politics are more prominent in Korea than Taiwan, but petty corruption has been largely eliminated. Both have set up and strengthened institutions responsible for fighting corruption. However, both democratic systems have reached the point where rival political parties use accusations of corruption against the other for political gain. These accusations could start hurting perceptions, as is happening in the US."

Taiwan's anti-corruption system remains fragmented

Further sustained improvement in Taiwan's score - and any hope of reaching the heights of Singapore, Australia and Hong Kong in these surveys - would likely depend in part on reviewing the island's anti-corruption institutional framework. As we noted in CG Watch 2020, there is no central independent agency such as the CPIB in Singapore or ICAC in Hong Kong, rather a more fragmented structure involving the public-sector ombudsman, the Control Yuan, and two other entities: the Agency Against Corruption (AAC), which acts as a judicial police authority and has prosecutorial power, and the Ministry of Justice Investigation Bureau (MJIB), which has wide powers of investigation and arrest relating to corruption in both the public and private sectors. These agencies are not independent of the government and there are lingering concerns that some cases have political overtones. On a more positive note, coordination between the AAC and MIJB does seem to be improving - although more transparency on their joint efforts would be welcome.

2. Regulators

Taiwan retained 2nd place on a slightly lower score of 65%

Taiwan lost a percentage point in score for Regulators but retained 2nd place, ranking equal with Japan on a score of 65%. Leading the pack in this category was Australia, which ranked third in 2020. A major reason for the reordering was a significant fall in Hong Kong's score from 69% to 62% and its drop in ranking from 1st to 5th.

Regulators have tried to imbue a deeper sense of CG in companies

On the positive side of the ledger, regulators pushed forward several upgrades to CG rules (see the next section) and tried to imbue a stronger sense among listed companies and institutional investors of the need for substance not just form in corporate governance - with understandably mixed success.

Regulatory websites are better

Other areas of improvement include the accessibility of laws and regulations on regulatory websites - although there is scope to make them even more user-friendly - and the archive of issuer announcements and reports provided by the TWSE.

Reform can still be piecemeal

We deducted points for limited consultation exercises and limited ambition in addressing some entrenched problems like related-party transaction regulation, legal-entity directors, and nomination committees. Despite the CG Roadmap, reform can still be somewhat piecemeal. Meanwhile, one area where transparency has not improved is the disclosure of regulatory funding and capacity building.

2.1 Funding, capacity building, regulatory reform

Taiwan slipped to equal 2nd place on a slightly reduced score of 61%

In line with its overall regulatory category score, Taiwan lost a percentage point in this sub-category, achieving 61% and slipping to equal 2nd with Australia. In 2020 it came equal 1st with Australia and Hong Kong. This time Hong Kong fell sharply while Japan surged to 67% and 1st place on the back of its broad and much bolder CG reform efforts, among other things.

Where scores rose

This sub-category has 11 questions and Taiwan gained points in three but lost in five. The improving scores covered the following questions: whether regulatory websites are informative and have English translations of key laws and regulations; whether the stock exchange provides an archive of issuer announcements and reports dating back at least 15 years; and to what extent the IPO regime encourages governance development in companies preparing to list.

Where scores fell

Questions where scores fell included: whether the securities commission is sufficiently resourced; the extent to which it is investing in new surveillance and enforcement capacity and technology; the extent to which the stock is investing in new capacity and technology; and efforts made by both the commission and stock exchange to modernise laws and listing rules, respectively, to improve CG.

Improving: TWSE website

The TWSE English website has clear links to key rules

We gave a slightly higher score for our question on regulatory websites in large part due to the TWSE site, which has a useful page called "Regulations". This leads to several sub-pages, the first of which is a "Rules & Regulations Directory" that provides quick links to news releases, laws, "categories" (ie, capital market sub-sectors and thematic areas such as corporate governance), and a search function. Links to the same pages are also provided in the dropdown menu under the initial Regulations tab, thus providing a degree of useful redundancy.

All key rules are accessible and up-to-date

A positive feature of these pages is that the information is largely up-to-date and in English. Separate links are provided to the Chinese version of each document. It is also possible to see the "legislative history" of a law or rule since enactment and which specific clauses of a regulation have been amended most recently (this format basically follows the "Laws & Regulations Database" run by the Ministry of Justice and is where one finds the Company Act and the Securities and Exchange Act). Despite these improvements, one still must work quite hard to find documents: most entries are organised either alphabetically or in no obvious order, requiring a lot of scrolling up and down the page. A table of contents organised thematically would help.

The FSC English website is not as useful for finding rules and regulations

We have not seen a similar improvement in the English homepage of the Financial Supervisory Commission (FSC). Although there is a prominent link to "Laws and Regulations", this leads to two pages called "Explanation of New Regulations" and "Preview of Law Draft" that do not appear to be complete or up to date. There are links to the three main supervisory bureaus for banking, securities and futures, and insurance, yet the Securities and Futures Bureau (SFB) link only takes one to the homepage of the "Law Source Retrieving System of Taiwan". While the latter is kept up to date, there is no page on the FSC website with a simple hierarchical list of key laws and regulations by subject/theme as one finds in other markets.

The SFB web pages are somewhat better, but not complete

The FSC website also has a link to a separate English homepage for the SFB, which is generally better organised. It also includes a tab called "Laws and Regulations" with a drop-down menu offering several options. The first is "Regulations" and leads to a page that appears not to have been updated since May 2021. Other links also lead to pages with little information on them, although one connects to the "Law Source Retrieving System of Taiwan". Although the Chinese pages of the FSC and SFB websites are thorough and timely, it would be helpful if the English pages were more comprehensive and up to date too.

Improving: Issuer archive

A huge improvement in the company archive, MOPS

We significantly increased the score for the stock exchange's archive of issuer announcements, reports, and notices. Called the Market Observation Post System or "MOPS" for short, we previously gave this a low 1 out of 5 for the lack of historical information in English, a poor search engine, and a hard-to-use design. We have increased the score to 3/5 because the organisation of material is vastly improved, there is new search function with the cute name of "ezSearch" that offers multiple subject categories and filters (which are easy to use), and there is much more information in English. A higher score in future would require, among other

things, an archive that goes back more than 10 years and all documents provided as promised (eg, while the search engine offers company prospectuses, it did not work in either English or Chinese for some companies we checked).

Improving: Pre-IPO governance

A bump in score for efforts to require listing candidates to do something on CG

Basic governance preparation in companies getting ready to list on stock markets around the region is generally poor in our view. Much more could be done before listing to train directors, appoint independent directors, set up functioning board committees, and ensure internal systems of control and risk management are fit for a public company. This should not be done a few months before listing, but one or two years before - it takes time to embed a modern governance culture and more sophisticated systems in companies. After reducing the score in 2020, we added a point this time for efforts made to require a degree of CG preparation by companies applying to the TWSE, Taipei Exchange (TPEx), or the Emerging Stock Board (ESB). For example, those listing on TWSE/TPEx must appoint at least three independent directors, who make up no less than one third of the board, before they apply; while those listing on the ESB must appoint at least two independent directors, who make up no less than 20% of the board, at least six months before they apply. Other rules relate to training in securities law or CG (at least three hours), the establishment of functional board committees for audit and remuneration, appointment of a CG officer (for TWSE/TPEx companies) and so on. This approach is a good start but could go a lot further.

Scores reduced: Regulatory resources and investment

Taiwan divulges less information than other leading markets on regulatory funding

We reduced scores for questions on the funding of the FSC/SFB and TWSE, and their investment in new technology, not because we believe they are insufficiently resourced but because their disclosure is significantly less than other leading markets. The FSC/SFB budget is somewhat confusing to understand, as brief information is provided on annual operational spending on the FSC website in addition to a much larger amount allocated to an entity called the "Financial Supervisory Fund", which is used for liquidating failed insurance and financial firms. In contrast, securities commissions in Australia, Hong Kong, India, Malaysia and Thailand provide a full set of accounts, while those in Japan and Korea provide more easily digestible figures than is available in Taiwan. The TWSE meanwhile does not provide hard numbers but says: "The TWSE has been performing well in the past, with sufficient profits and retained earnings to cover the cost of supervisory and law enforcement personnel."

Only qualitative information available on capacity building and new tech

As for investment in new surveillance and enforcement technology and capacity, the FSC provides brief information while the TWSE gives a qualitative summary. For example, the exchange's Corporate Governance Department, which was established in 2014, saw staffing numbers increase by 50% to support its work on ESG and sustainability.

Scores reduced: CG reform

Regulatory reform efforts are strong, yet would benefit from more consultation

It may seem somewhat perverse to downgrade Taiwan's scores for CG reform (Q2.5 and Q2.6) in our latest survey, since regulators have been working hard to fill gaps in the regime and have made solid progress in addressing some longstanding concerns. Nevertheless, we cut a point for the regulatory efforts of both the securities regulators and the stock exchange for the reason given earlier: that new rules are sometimes hastily adopted and not as well-crafted as they could be. Taiwan still scored 4 out of 5 for each question, reflecting good performance overall, yet continues to do poorly on a question (Q2.7) relating to the effectiveness of the public consultation system.

Too hasty: virtual AGM rules

Rules on virtual AGMs introduced too quickly

One area where rules were introduced somewhat hastily in our view relates to virtual annual general meetings. Prior to Covid-19, Taiwan did not have rules permitting either virtual or hybrid meetings, a point we highlighted in CG Watch 2020. This caused problems for Taiwan's AGM season in mid-2021, after which authorities moved swiftly to amend the Company Act and Regulations Governing the Administration of Shareholder Services of Public Companies. The new rules came into force in March 2022 in time for that year's AGM season.

Taiwan limits the content of virtual and hybrid meetings

While authorities are to be commended for addressing this problem, certain aspects of the rules remain problematic. For example, issuers can amend their Articles of Incorporation by a simple board resolution to allow virtual-only meetings at any time, not just during exceptional circumstances such as a pandemic. As ACGA noted in a commentary later in 2022, this necessitated introducing some guardrails to "prevent Taiwan's notoriously inventive blockholders from gaining an upper hand in battles for management control". The answer was unorthodox and involved setting limits on the content of meetings. Specifically, virtual-only meetings cannot vote on resolutions relating to director or supervisor elections or dismissals ("discharges"), or on M&A activity. If meetings are hybrid, director and supervisor elections are permitted but only if they are uncontested. Dismissals are not allowed. Our concern is that if there is another pandemic and all AGMs need to go fully virtual, these rules will almost certainly create problems for companies and tension with shareholders - especially if the pandemic year happens to align with the re-election of directors and supervisors.

A longer and more intensive consultation period would be beneficial

A public consultation was held on these new rules in early 2022, but it was relatively short (only 30 days), and the rules appeared to come fully baked in the "Preannoucement" on 21 January 2022 (ie, it seemed unlikely that any market feedback would change the rules substantively). In addition to a longer and more open consultation period in future, we recommend that authorities seek detailed input from key stakeholders, including foreign shareholders, before finalising rules that directly affect them.

2.2 Enforcement

Taiwan retained the same score of 70% but dropped two places to 4th

Enforcement is the main category in our survey where differences in score between markets are the smallest. Taiwan retained its previous score of 70% but dropped from equal 2nd with Singapore in 2020 to 4th in 2023. The standout leader previously, Hong Kong, held on to 1st place but with a reduced score of 72%, putting it on a par with Australia. Singapore gained a point to 71% though slipped to 3rd place. Notably for Taiwan, fewer individual ratings changed in this sub-category than in the previous one: out of 10 questions, three improved and two fell.

Where scores rose

We gave higher scores for the reputation of regulators for enforcement and whether their efforts have been improving and evolving; and for the range of powers that the stock exchange can apply to enforcing its listing rules.

Where scores fell

We cut scores on the disclosure of multi-year enforcement data by both the securities commission and the stock exchange because the presentation of this information is not as complete as other markets, and it is not easy to find the outcomes of criminal prosecutions.

We assess Taiwan's regulatory agencies as a whole, including MJIB and the SFIPC, in this category

It is worth noting that Taiwan scores highest (5 out of 5) for whether financial regulators have robust powers of surveillance, investigation, sanction, and compensation. We take a systemic view and include the MJIB and SFIPC as well as the FSC/SFB when answering this question. Enforcement powers tend to be more distributed in Taiwan than in other markets such as Australia and Hong Kong where they are centralised in securities commissions, or in Japan where they are vested in the securities commission and a related agency. In Hong Kong, for example, the Securities and Futures Commission has the power to litigate and seek compensation on behalf of minority shareholders, while in Taiwan this role is undertaken by the SFIPC, which has a much broader remit in this area than the HKSFC.

Taiwan regulators coordinate closely with other enforcement arms of government

Taiwan has also typically done well (scoring 4 out of 5) on whether the financial regulator receives committed support from other enforcement arms of government. Cases typically start after the TWSE or TPEx find evidence of a violation of the law through their supervision of market trading and issuer disclosure - or enforcement bodies such as MJIB receive media reports or a whistleblower tip-off. The TWSE and TPEx then report to the SFB, which may issue an administrative penalty. If there is evidence of criminal wrongdoing, cases will be sent to the MJIB or prosecutors. The FSC/SFB is assisted in their initial investigation of criminal cases by prosecutors embedded in the regulator. Each entity above has a clearly defined role, as does the SFIPC, which may launch a parallel civil action against a violator. The reason Taiwan does not score a 5/5 is because the court system can be inefficient and has often produced inconsistent judgements in the past, a problem that the new Commercial Court is helping to resolve.

Rising scores

A higher rating for enforcement vigour and consistency

Taiwan received a half-point bump for Q2.12 on whether regulators have a reputation for vigorous and consistent enforcement, rising to 3.5 out of 5. This was in part due to several cases that helped to firm the regulator's reputation, including Taisun vs Long Bon, the Catcher AGM case, and Pharmally. The FSC coordinated well with the Ministry of Economic Affairs on the Catcher case. The higher score was also because the FSC chairman, Huang Tien-mu, had been in position for 3.5 years at the time of our assessment - a relatively long period of time for someone in this role in Taiwan. He has impressed with his consistency. Huang's term ended on 19 May 2024, and he has been succeeded by Peng Jin-lung, associate dean of the College of Commerce at National Chengchi University. Peng has also served as a director of several insurance companies and banks. Peng assumed his new role on 20 May 2024, the same day as the new President, Lai Ching-te, took office.

Enforcement efforts are evolving to meet current needs

A full additional point was given for Q2.13 on the extent to which enforcement efforts are improving and evolving. The new Commercial Court is not only making the work of the SFIPC more effective, but the latter gained new powers to monitor AGMs in June 2022. This not only allows it to attend physical or hybrid/virtual meetings and ask questions, but it can also issue press releases beforehand on areas of concern and later if it feels it has more to say. It selects the AGMs to attend based on companies that scored poorly in the annual Corporate Governance Evaluation exercise undertaken by the TWSE. Meanwhile, we see much more enforcement data from regulators - five-year historical figures are provided - with some trend analysis and case studies of major prosecutions.

A bump too for the powers of the stock exchange

We also added a half point for Q2.17 on the enforcement powers of the stock exchange, taking the score to 4.5 out of 5. Taiwan gained on the ability to impose administrative remedial measures on issuers - in addition to other powers such as

private/public reprimands, fines, and suspensions that were previously recognised in our score. Unlike the Hong Kong Exchange, for example, the TWSE does not take remedial actions such as imposing a director-training requirement for incompetent boards of companies. It does, however, issue "letters of correction" requesting companies fix disclosure deficiencies in their financial statements and internal control system audits. It also requires companies with poor operations and finances to make periodic disclosures of their financial condition. For these reasons, we reassessed our score on remedial measures and added a point. On the other hand, we cut half a point for relatively weak use of public censures.

Falling scores

Enforcement data is good, but not as good as some other leading markets

The two questions where scores fell, by a point each, were for the disclosure of enforcement data by regulators and the stock exchange. Despite some genuine improvements in this area over the past few years, the disclosure regime is still not as complete or compelling as other leading markets. We therefore felt that, objectively speaking, lower scores were warranted.

An annual enforcement report gives a very good overview of the work of key agencies

What has improved? Since 2019 the FSC/SFB has been producing an annual "Law Enforcement Report" covering the work of TWSE, TPEx, the Taiwan Futures Exchange Corporation, MJIB, and the SFIPC. It is now a detailed report of almost 80 pages, with recent versions showing an improvement in data presentation and general readability. Statistics in the latest 2022 report are provided for five years (2018-2022) compared to three years in the 2020 report (2018-2020). There is a helpful analysis of trends in the data (eg, why certain types of sanctions have been rising or falling) and detailed examples are provided of major criminal or civil cases during the year. All in all, it is a handy and informative document that gives a solid overview of how financial regulators have approached enforcement and what they have achieved. It is also worth noting that while the 2020 report took almost 12 months to publish, the next edition took 10 months and the latest only eight months. (The 2023 edition has yet to be released.)

But disclosure of the outcome of individual criminal cases is still not as complete in Taiwan as other markets

What are the shortfalls? The main issue is something we also see in Japan, namely the lack of timely and complete announcements from regulators on all types of individual enforcement cases. In markets like Australia, Hong Kong and Singapore, financial regulators publish detailed press releases when charges are laid against individuals or companies for criminal or civil breaches of securities laws, provide updates as relevant, and then final announcements when penalties are meted out or cases later decided by courts. In Taiwan, the SFB publishes quite detailed announcements whenever it issues administrative fines, warnings or other sanctions. There are no links, however, to press releases on the outcomes of criminal cases. Some cases will get a vignette in the MJIB annual report, and the Ministry of Justice publishes voluminous statistics on all forms of criminal investigations, prosecutions and convictions. Yet there is not a specific online resource providing announcements on what happened in individual cases relating to criminal breaches of company or securities law. It is possible to search through the results of court cases to find out the rulings, but this is not easy and does not include information on when cases were dropped or why. (Note: Since 2021 the SFIPC has provided a list of "Major Securities and Futures Illegal Cases" under the class action section of its website. This very briefly summarises the progress and outcomes of criminal prosecutions, but only for cases where the Center has filed a civil suit. As of end-May 2024, there were 26 such cases listed.)

Nor does TWSE enforcement disclosure match its counterparts

The TWSE, meanwhile, releases statements on the penalties it imposes for violations of listing rules, but these can be extremely brief. For example, "TWSE imposed NT$50,000 breach penalty on XXX Co., Ltd for violating the regulations involving internal control." There are somewhat more detailed explanations as to why the exchange imposes trading controls on issuers experiencing unusual trading activity (ie, "attention" and "disposition" securities). But there is nothing like the level of enforcement detail and narrative one finds, in contrast, on the website of the Stock Exchange of Hong Kong.

What the enforcement numbers say

Taiwan regulators do try to explain changes in enforcement data

The Law Enforcement Report for 2022 contains a rich data set on enforcement trends over the period 2018 to 2022 and provides a concise explanation for changes in the numbers - something most regulators are not particularly good at. Figure 20 summarises the number of sanctions, actions and penalties issued by the key regulatory agencies over the five years.

Figure 20

Enforcement actions in Taiwan, 2018 to 2022

Unit	Action	2018	2019	2020	2021	2022
SFB & FSC	Sanctions (No. of cases)	293	357	351	367	287
	Aggregate penalties[1] (NT$m)	65	82	104	87	68
MJIB	Criminal investigations (No. of cases)	61	60	57	49	63
	Proceeds of crime[1] (NT$bn)	20.1	16	16.6	11.7	5.2
SFIPC	Class-action suits (No.)	10	12	10	11	7
	Compensation sought[1] (NT$bn)	1	1.7	0.7	7.2	7.3
	Derivative suits (No.)	5	2	6	8	9
	Discharge suits (No.)	9	5	7	6	14

[1] Figures rounded. Source: FSC/SFB, Law Enforcement Report, 2022

Key reasons for the changes in some of these numbers include:

- SFB penalties started rising in monetary terms 2019 because the ceiling for administrative sanctions increased from NT$2.4m (US$80,000 approx) to NT$4.8m and securities firms were subject to a new rule on internal controls. The number of sanctions fell in 2022 mainly due to fewer breaches of securities disclosure rules by insiders.
- MJIB criminal investigations declined from 2018 to 2021 primarily because of lower numbers of stock price manipulation cases, "unconventional transactions", and breach of trust and embezzlement. At the same time, insider trading investigations jumped significantly in 2021. Numbers rose in 2022 as more cases appeared in stock manipulation, counterfeit documents, and insider trading. Proceeds of crime dropped for a range of reasons. In stock manipulation, for example, the number of cases and suspects rose in 2022 but the proceeds of crime fell because many of these trades ended in failure with the criminals losing money.
- SFIPC class-action lawsuits fell somewhat in 2022 due to certain difficulties faced in setting up cases for insider trading and stock manipulation. On the other hand, discharge suits against directors and supervisors effectively doubled in 2022. As the SFIPC told ACGA, the number of discharge suits is mainly affected by the number of illegal cases received from prosecutors or relevant institutions. Meanwhile, the Center's new policy on discharge suits, which is to file suits against directors even if they have resigned from boards, is one of the factors for their rise in significance.

While the Law Enforcement Report is an extremely useful document, and one that other markets could well emulate, we would encourage Taiwan regulators to publish more timely and complete enforcement announcements on their websites. Closing the loop on criminal prosecutions would also be useful.

3. CG rules

Taiwan remained 7th while improving its score to 71%

In percentage terms, CG Rules was one of Taiwan's most improved categories: its score jumped from 66% in 2020 to 71% in 2023. Its 7th place ranking did not change, however, reflecting stiff competition in this area. The improved score was largely a result of efforts made by Taiwanese authorities to address some longstanding shortcomings in the regulatory environment.

Scores increased on 8 questions

Scores increased on questions relating to disclosure of substantial ownership (the 5% rule), disclosure and approval of related-party transactions, closed periods for director trading prior to the release of financial results, overall corporate reporting standards, deterrents against insider trading, voting by poll, the Stewardship Code, and the release of proxy materials prior to AGMs.

Scores fell on 3 questions

Scores fell on three questions: disclosure of share pledges by controlling shareholders; nomination of directors by minority shareholders; and pre-emption rights for minority shareholders.

Improvements in sustainability reporting rules did not lead to a higher score - Taiwan already gets full marks

It is important to highlight that there were some areas in CG Rules where Taiwan already achieves full marks, hence scores did not increase despite an improvement in the regulatory environment. A good example is sustainability reporting. However, we did reflect Taiwan's strong performance here in the Listed Companies survey. There were other areas, such as CG reporting and the CG Code, where scores did not increase despite some improvements in rules or guidance. We left scores the same because we felt that Taiwan was still fairly rated compared to other markets, some of which are either moving ahead faster or have more complete reporting systems.

The 5% rule *(Question 3.05)*

At long last, the 5% disclosure rule has arrived

An amendment to rules on the disclosure of substantial ownership have been long-awaited in Taiwan. Historically the threshold has been set at 10%, which is out of kilter with the 5% found in most of Asia and other developed markets around the world. Following approval by the Legislative Yuan, the government promulgated an amendment to Article 43-1 of the Securities and Exchange Act (SEA) on 10 May 2023 bringing the level down to 5%. The new rule took effect exactly one year later, while existing shareholders with stakes of 5%-10% were given a further year to adjust their positions so as to lessen potential selling pressure on the market.

But disclosure is still at 10 days

While this change is significant, we remain concerned that peculiarities of the Taiwan system will continue to obstruct full transparency. For example, the timing of disclosure remains at 10 days, whereas we believe it should be no more than five days. (Note: This rule can be found in Article 6 of the "Regulations Governing the Declaration of Acquisition of Shares in Accordance with Article 43-1, Paragraph 1 of the Securities and Exchange Act".) More positively, the 1% "creeper rule" requires disclosure within two days (see Article 7) and the regulator has prepared guidance for companies on how to follow the new rules. Given the slow disclosure on 5% stakes, however, and that fact that the new rule had not come into effect when we were scoring for CG Watch 2023, we only increased the score by a point to 2 out of 5.

Related-party transactions *(Q3.10)*

Tougher rules announced on RPTs in January 2022

In January 2022, ACGA sent a letter to the SFB in response to its "Proposed Draft Amendments to Regulations Governing the Acquisition and Disposal of Assets by Public Companies". We welcomed the proposed amendments as a step towards enhancing the regime for the disclosure and approval of related-party transactions (RPTs). There is a new shareholder approval requirement, for example, for transactions that reach 10% or more of a public company's total assets. There are also complementary changes to the CG Best Practice Principles extending the scope of RPTs to goods and services, loans and endorsements, and a call to report these to the AGM or seek shareholder approval.

The amendments do not go far enough, in our view

The amendments do not go far enough, however, in addressing the fragmented nature of the RPT disclosure system in Taiwan. Transactions within the same corporate group are still exempt from a shareholder vote. The rules do not apply to goods and services or loans and endorsements. And the 10% threshold for a shareholder vote is extremely high. Meanwhile, the changes to the CG Best Practice Principles, although positive, lack specifics and are not hard rules. For these reasons, we only increased the score a point to 2 out of 5. Compared to the comprehensive RPT disclosure and approval regimes one finds in other Asian markets, we concluded that Taiwan is not yet halfway there. Indeed, this was another area where we felt rule amendments were somewhat rushed and would have benefited from a deeper and longer market consultation.

Trading blackouts *(Q3.08)*

There is now best-practice guidance on when directors should be allowed to trade

Taiwan received a bigger boost to its CG Rules score for introducing guidance on when directors should and should not trade shares prior to the release of financial results. While there is still no hard rule on this issue, the CG Best Practice Principles were updated on 8 December 2021 to call on issuers to prohibit directors from trading their shares during a closed period of 30 days prior to the publication of the annual financial reports and 15 days prior to the publication of the quarterly financial reports. We duly increased the score from zero to 1.5 out of 5. Had this been a rule change, we would have scored this question 2.5 out of 5. The reason for not going higher is that 30 days is precisely half the best-practice benchmark set by Hong Kong of 60 days before the release of annual results.

Adjusting up

Scores raised for corporate reporting standards, insider trading, voting by poll, Stewardship Code, and AGM proxy materials

Reasons for upward adjustments on five other questions included:

- **Corporate reporting standards *(Q3.01):*** We reassessed our previous downgrade for the full annual reports of all listed companies not being required until seven days before the AGM. In our 2020 survey we deducted a full point for this rule, but adjusted it to a more reasonable half-point reduction this time. The rules have also tightened in this area. Prior to 2021, companies with a paid-in capital of NT$10 billion or more were required to release their annual reports two weeks before their AGM. In that year a further stipulation was added: that companies with foreign and Mainland Chinese shareholdings exceeding 30% must also do so. Then in November 2023, the paid-in capital threshold was lowered to NT$2 billion or more. This will apply from 2024.

  We also noted that the TWSE and TPEx amended their listing rules in April 2021 to require companies with paid-in capital of NT$10 billion or more to release their "self-assessed" (unaudited) annual financial information within 75 days of the end of the fiscal year, starting in 2022 - as opposed to the three months given for the released of audited annual results. This new rule was extended to all listed companies in two stages over 2023 and 2024. Meanwhile,

the FSC promulgated an amended regulation in April 2021 requiring large companies with NT$10 billion paid-in capital or more to release their audited annual financial reports within 75 days starting in 2023.

- **Insider trading *(Q3.11):*** While the law and criminal penalties on insider trading have not been amended for some time, the SFIPC gained new powers in 2020 to seek the discharge of directors involved in such cases. The ban from the company is for three years and the Center has started to take action. We added half a point for progress to date.
- **Voting by poll *(Q3.12):*** In 2020 we deducted a full point because the meeting minutes of the AGM did not include disclosure of any Q&A with shareholders - a practice that had become the norm at the time in other parts of the region, such as Thailand and Malaysia. We added half a point because this practice is now encouraged in the TWSE's CG Evaluation system: Item 1.18: "Did the company record in the AGM minutes the important contents of shareholders' questions and the company's replies?" This took Taiwan's score to 4.5 out of 5. It still falls slightly short of full marks because any independent vote scrutineers appointed by the chairman "shall be shareholders of the company" (Article 15 of the "Rules of Procedure for Shareholder Meetings"). We prefer fully independent scrutineers.
- **Stewardship Code *(Q3.14):*** We gave a half-point increase in score to 4.5 following revision of the Code to encourage institutional investors to disclose voting down to the individual company and resolution level.
- **AGM proxy materials *(Q3.22):*** In 2020, the final AGM "handbook" containing the meeting agenda and all necessary supporting materials only needed to be released in electronic form 21 days before the meeting - a week short of our 28-day benchmark. The TWSE raised the bar in December 2021 to 30 days for large listed companies with a paid-in capital of NT$10 billion or more, or which had 30% or more foreign or Mainland Chinese investors on their shareholder registers. In December 2023, the 30-day threshold was lowered to companies with paid-in capital of NT$2 billion or more. Although the rule does not yet apply to all listed companies, 86% of them already meet it. Taiwan now scores full marks on this question.

Adjusting down

Reasons for reducing scores on three questions included:

Scores reduced on share pledges, director nomination, and pre-emption rights

- **Share pledges *(Q3.07):*** Disclosure of share pledges is required of directors, managers and 10% shareholders: "When the shares referred to in the first paragraph hereof are pledged, the pledgor shall make immediate notification to the issuer; the issuer shall inform the Competent Authority of such pledges within five days of their formation, and publicly announce such pledge." However, disclosure is only required within five business days, which is slower than our standard of three days (for this reason we deducted a point in our 2020 survey). We cut a further point this time because corporate control can be achieved in Taiwan at less than 10% and this rule has not been amended to align with the new 5% substantial ownership rule. Poor disclosure of beneficial owners coupled with legal-entity directors often makes it hard to figure out who is a controlling shareholder in Taiwan. The score was cut to 3 out of 5.
- **Nomination of directors *(Q3.19):*** While Taiwan has one of the region's more liberal systems for the nomination of directors by minority shareholders, it does not require the name of the proposer to be included in the AGM proxy form. Since this is material information and standard in most other markets, we deducted a point, lowering the score to 4 out of 5.

- **Pre-emption rights *(Q3.21):*** We slightly reduced the already low score here of 2/5 by half a point because insiders (directors, supervisors, management officers, shareholders owning more than 10%, and "any spouse, minor child, or nominee holder thereof") are allowed to participate in private placements if a company is not profitable. This seems to offer a loophole for insiders to extend control of listed companies at a cheap price during difficult times.

  Taiwan's rules in this area are quite convoluted and found in both the SEA (Article 43-6) and the TWSE's "Directions for Public Companies Conducting Private Placements of Securities". They are both stricter and more lax than the more straightforward rules operating in markets such as Hong Kong, which we hasten to add scores poorly on this question too (2/5) - as do most markets except for Australia, Malaysia and Singapore, which do a little better.

  Positively, Taiwan's rules state a preference that profitable listed companies should raise capital through public offerings unless necessity forces them to do so privately. Shareholder approval is required at a higher threshold: a two-thirds vote on a quorum of shareholders representing a majority of issued shares - as opposed to the simple majority in Hong Kong with no significant quorum. And placees are subject to three-year lock ups.

  Negatively, there is no volume limitation in Taiwan - best practice elsewhere is no more than 5-10% of issued capital per year. No maximum price discount - best practice is no more than 5-10% of the recent average share price - though TWSE rules do effectively say that if the discount is more than 20% then an independent expert opinion is required before shareholders vote. And private placements can be used to introduced a strategic investor, with the possibility that this could lead to a change in control of the business on unfair terms to minority shareholders.

Sustainability reporting: upping the climate ante

Improvements in ESG reporting led to higher scores in Listed Companies

Since Taiwan already achieved full marks in our last survey for sustainability reporting, as noted above policy improvements made in recent years had no impact on its overall score this time in CG Rules. They did, however, lead to higher scores for ESG disclosure in the Listed Companies section.

Taiwan was an early mover in sustainability reporting

Taiwan was an early mover in sustainability reporting following the tainted food (cooking oil) scandal of 2014. It began mandating GRI for firms in high-risk sectors (F&B, food, chemicals) as well as finance/insurance and large firms with NT$10 billion or more in paid-in capital from that year. It steadily expanded the reporting net to firms with lower paid-in capital levels, extending it to issuers with more than NT$2 billion in paid-in capital from 2023. And from 2025 all listed companies will have to issue full sustainability reports. These rules are found in the TWSE's "Rules Governing the Preparation and Filing of Sustainability Reports", which have been amended multiple times since 2014 and most recently in January 2024. The requirement is for reports in Chinese.

"Sustainable development" has been national policy since 2010

Companies must also disclose on a "comply or explain" basis in their annual reports the extent to which they follow the "Sustainable Development Best Practice Principles for TWSE/TPEx Listed Companies". Promulgated in February 2010, these principles have also been amended several times, most recently in December 2022. The intention is wide-ranging: to "encourage TWSE/TPEx listed companies to actively fulfil sustainable development in the course of their business operations so as to follow international development trends and to contribute to the economic development of the country, to improve the quality of life of employees, the

community and society by acting as responsible corporate citizens, and to enhance competitive edges built on sustainable development". In this sense, the recent national Sustainable Development Guidemap" is not entirely new.

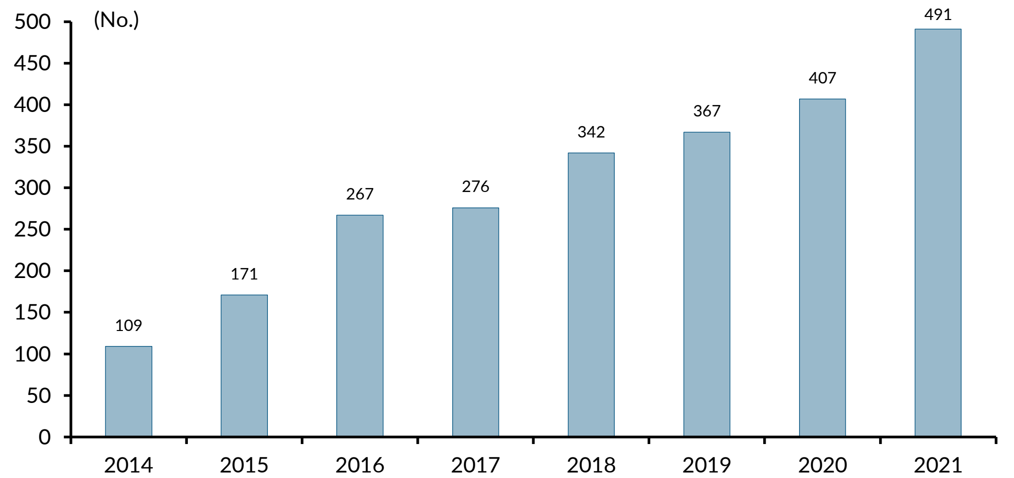
Taiwan was also an early adopter of ESG assurance

Taiwan has also been a speedy adopter of ESG assurance - quite a bold step given how tentative most markets have been on this issue (with the exception of India). As early as 2021, half of all TWSE-listed companies (491 issuers) had published ESG reports and 68% of them had some form of third-party assurance. See Figures 21 and 22.

Number of issuers releasing ESG reports has been steadily rising

Figure 21

Number of TWSE issuers publishing ESG reports, 2014 to 2021

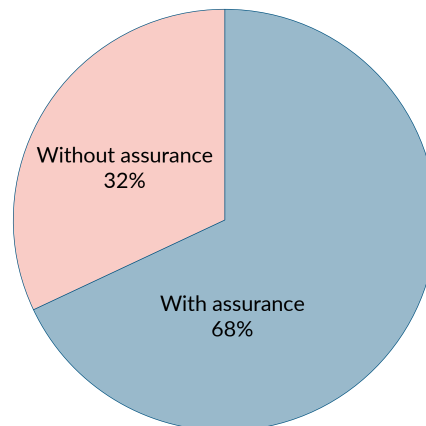


Source: TWSE

Most ESG reports are assured to some degree

Figure 22

Proportion of ESG reports assured, 2021



Source: TWSE

A focus now on climate reporting and assurance

In addition to expanding the scope of sustainability reporting to more listed companies, the other big change in recent years has been the addition of climate reporting and assurance for both financial firms and listed companies. The Green Finance Action Plan 3.0 encourages financial institutions to "disclose and verify" Scope 1, 2 and 3 emissions. They should also set medium and long-term carbon reduction strategies and objectives, including using their client relationships to influence the plans of investees and borrowers.

Issuers must disclose in line with TCFD from 2023

Specifically for listed companies, the TWSE and TPEx announced amendments in September 2022 to their "Rules Governing the Preparation and Filing of Sustainability Reports" stating that issuers would be required to disclose climate-related risks and opportunities based on the TCFD framework from 2023. Secondly, certain industries will also have to report on sustainability metrics by industry: initially those in food, chemicals, finance/insurance, and companies which derive at least half their operating revenue from food and beverage. These companies will also have to obtain a "letter of opinion" from a certified public accountant on their sustainability metrics. The rules go on to list another 14 industry sectors, such as cement, plastics, iron and steel, that must also "strengthen the disclosure of sustainability metrics by industry" - although they are not required to have their reports assured. The starting dates for this reporting are either 2023 or 2024 depending on paid-in capital amount and the rule changes come with a series of appendices listing sustainability metrics by industry, based on SASB standards.

Firm dates for GHG inventory reporting and verification

Importantly, the amendments introduce a new section to the Rules (Article 4-1) outlining a series of dates by when listed companies must disclose their Scope 1 and Scope 2 carbon emissions data, called "GHG inventory" in Taiwan, and have this data "verified". As Figure 23 shows, larger companies and those in steel and cement must start reporting from 2023 and have their numbers verified from 2024. All listed companies will be reporting by 2027 and all must have their inventories verified by 2029.

Figure 23

Phasing in GHG inventory disclosure and verification in Taiwan, 2023 to 2029 - framework for listed companies

	2023	2024	2025	2026	2027	2028	2029
GHG inventory	Companies with paid-in capital of more than NT$10bn + those in steel and cement		Subsidiaries of companies with paid-in capital of more than NT$10bn + steel and cement + Companies with paid-in capital of NT$5bn to $10bn	Subsidiaries of companies with paid-in capital of NT$5bn to $10bn + Companies with paid-in capital of less than NT$5bn	Subsidiaries of companies with paid-in capital of less than NT$5bn		
Verification		Companies with paid-in capital of more than NT$10bn + those in steel and cement			Subsidiaries of companies with paid-in capital of more than NT$10bn + steel and cement + Companies with paid-in capital of NT$5bn to $10bn	Subsidiaries of companies with paid-in capital of NT$5bn to $10bn + Companies with paid-in capital of less than NT$5bn	Subsidiaries of companies with paid-in capital of less than NT$5bn

Source: Financial Supervisory Commission; ACGA table

Climate reporting also added to rules on annual report disclosure

Then in late November 2022 the FSC put all of the above on a firmer governance footing by announcing important amendments to rules on annual reports. It amended the "Regulations Governing Information to be Published in the Annual Reports of Public Companies" by adding a new appendix titled "Climate-Related Information of TWSE/TPEx Listed Company". The first part requires disclosure of the oversight by the board and management of climate risks and opportunities, how these factors affect the business, strategy and finances over the short, medium and

long-term, and another seven factors largely in line with TCFD. The second part lays out specific pointers for the disclosure of GHG inventory and assurance for the most recent two fiscal years. And the third and final part outlines requirements for disclosure of a GHG reduction plan and targets. The start date for this new disclosure was set at 1 January 2024.

Taiwan also has rules on who can do assurance of sustainability reporting

Who can do assurance?

Unlike most markets, where little regulatory thought has been given as to who should do the verification or assurance of sustainability reporting, Taiwan also has a plan for this. According to the "Directions for the Implementation of Assurance Institutions for the Sustainability Report of TWSE/TPEx Listed Companies", assurance is divided into two groups:

1. For sustainability indicators in mandatory ESG reports, only CPA firms are permitted to undertake assurance. They must follow the ISAE 3000 standard.
2. For verification of GHG emissions, the work can either be done by CPA firms using the ISAE 3410 standard or by specialist consultants approved by the Environmental Protection Agency (EPA) and using the ISO 14064-3 standard. In April 2024, ARDF released the TWSAE 3410 assurance standard, which references ISAE 3410.

The rules became effective in January 2023

The Directions were announced on 21 December 2022 and became effective a few days later on 1 January 2023.

CG Best Practice Principles have been updated several times in recent years

CG Best Practice Principles

One recurring theme in all sustainability regulation and guidance from Taiwan regulators is repeated reference to either the "Corporate Governance Best Practice Principles" or practical examples of good governance on the TWSE CG Center website. While it is fair to say that most regulatory energy in recent years has been expended on sustainability matters, the CG Principles have been updated several times since our last survey. The main changes (with announcement dates in brackets) include, in brief:

- **Restrictions on trading by directors and insiders** (8 December 2021): introduced the "closed period" of 30 days prior to the announcement of annual financial results and 15 days before quarterly results, as outlined above in CG Rules.
- **Director remuneration disclosure** (8 December 2021): companies should disclose the "remuneration received by directors, including the remuneration policy, individual remuneration package, amount, and association with outcomes of performance reviews" at a general shareholders' meeting.
- **Board diversity** (8 December 2021): one-third of directors should be women.
- **Director tenure** (8 December 2021): independent directors should not exceed three consecutive terms of three years each (ie, nine years).
- **Shareholder meetings** (8 March 2022): should now allow for videoconferencing (ie, to support the new rules on virtual and hybrid AGMs).
- **Related-party transactions in M&A deals** (25 December 2022): if the management or major shareholders of a listed company is involved in an M&A deal, then a legal opinion should be issued by an independent lawyer to opine on the independence of the audit committee reviewing the transaction.

- **Other measures: CG officers; RPTs; audit committees; AQIs** (23 December 2022): Scope of work of CG officers expanded and related-party transactions extended to cover purchase and sale of goods, loans, endorsements and guarantees. Listed companies must establish an audit committee - they no longer have the option of a supervisor after 2022. And listed companies must assess the independence of their accounting auditor at least once annually with reference to the new Audit Quality Indicators (AQIs).

Although detailed, the CG Principles remain quite abstract and say little of local CG challenges

Taiwan's efforts to keep its CG Principles up to date, and take account of international norms, ensure it scores well on the related question (Q3.13) in our survey. It received a 4 out of 5 in both our 2020 and 2023 editions. The score has not increased, however, because while the Principles are detailed they also remain quite abstract. One does not learn much about local CG challenges from reading them. In contrast, Japan's CG Code includes commentary on a wide range of local issues, then attempts to provide solutions to these problems.

Taiwan and ISSB

Taiwan is attuned to new global sustainability reporting standards

Like other leading markets in Asia, Taiwan has been closely following developments at the International Sustainability Standards Board (ISSB) and its publication in late June 2023 of new global sustainability reporting standards. Not surprisingly, Taiwan has a fairly clear plan for aligning with ISSB standards. It established a taskforce in the second half of 2023 under the chairmanship of the SFB to undertake outreach to stakeholders, manage public consultations, and produce guidance and best practice examples. Its goal is to complete the translation of standards in 2024, develop training programmes in 2025, and require large caps to prepare sustainability information in line with ISSB by 2026 and report it in 2027.

Authorities formed an ISSB taskforce in 2023

The task force has four groups:

1. Group 1 on Standards Adoption: led by the Accounting Research and Development Foundation (ARDF), it is also in charge of translation.
2. Group 2 on Transition Aid: led by the TWSE, it will provide guidance and best practice resources.
3. Group 3 on Regulatory Amendments: led by the SFB, it sets the adoption roadmap and will align regulations with ISSB.
4. Group 4 on Promotion and Training: led by TPEx, it will organise seminars and training courses.

Taiwan is under no illusions that it needs much greater professional talent in the accounting and auditing industry to undertake all this work.

4. Listed companies

Taiwan's ranking fell to 5th on a much lower score of 55%

In line with many markets, Taiwan lost points in Listed Companies following a substantially revised and more concise survey of CG disclosure and practices. It dropped eight percentage points to 55% in large part because on many issues companies disclose what the regulator expects and little more. Its ranking also fell, from 4th in 2020 to 5th in 2023. Nevertheless, there are several areas where Taiwan also rated well or above average.

The 15 firms surveyed represented a range of sectors

For this section we surveyed in depth the governance practices and disclosure of 15 large caps selected from the top 50 listed companies. These firms represented a range of sectors: semiconductors, telecoms, autos, banking and finance, electronics, petrochemicals, and retail/consumer. Both English- and Chinese-language materials were reviewed.

Where Taiwan does well or above average (3 to 5 out of 5)

Companies score highest in sustainability reporting

Taiwan's large companies do best in sustainability reporting, earning an average score of 4.5 out of 5. This is as much a product of government policy, as outlined above under CG Rules and Government & Public Governance, as efforts made by companies on their own. Large caps and those in certain industries have had to follow GRI reporting standards for a decade and are under constant pressure to up their game in newer areas such as TCFD and SASB. Materiality reporting is broadly sound and companies are starting to discuss climate risk from a materiality perspective. Few however report the impact of climate-related matters on their financial performance. Overall, eight of 15 companies scored full marks (5 out of 5) on this question. Another four scored 4 or 4.5.

Companies excel also at investor relations

Most companies excel at investor relations (IR), with seven scoring full marks, another three scoring 4/5, and the remaining five either a 3 or 3.5. IR pages on websites are easily accessible, providing key financial, annual and sustainability reports (although the latter are sometimes in separate ESG or sustainability sections). Announcements and AGM materials are either available on company websites or the TWSE archive called "MOPS" (see above under Regulators). And, unusually for the region, quite a few Taiwan companies provide names and contacts details for their IR team - a simple but effective way to encourage greater communication with shareholders. We wished more companies around the region did the same.

Most independent directors are paid cash fees, while only a few receive a % of earnings

Pay for independent directors is mostly straightforward and comes in the form of a monthly cash fee - little room there for conflicts of interest. Of the 15 companies surveyed, 10 of them earned full marks, driving up the overall score. Notably, the remainder all scored poorly (1 out of 5) because they pay their independent directors a percentage of company earnings. We believe that such compensation practices potentially undermine the objectivity of these directors and hence their ability to challenge management.

Audit committees are mostly independent and financially literate

Audit committees generally have a high level of independence in terms of their membership as well as expertise in accounting and financial management matters. Many are independently led, with quite a few chairmen being accountants. Three companies earned full marks on this question, while another five scored 4/5. The remainder scored less either because their independence or expertise was slightly lacking.

Good disclosure on the relationship between internal audit and the AC

Companies also provide helpful disclosure on the relationship between their internal audit departments and audit committees. Not only do all companies have an internal audit department with a direct reporting line to the AC or independent directors, but many of them provide helpful summaries of issues covered by this communication. Taiwan remains unusual in encouraging this level of internal reporting - a practice we welcome - although it must be said that many issuers still provide only a generic list of topics.

Diversity policies are reasonably substantive

Board diversity policies are mixed, with one company scoring full points but many getting 3 and some 2.5. On the plus side, policies are reasonably substantive and provide sensible targets, while many companies also produce a skills matrix. On the other hand, targets are often limited to gender diversity rather than broader measures of diversity and/or merely follow regulatory requirements on gender, proportion of INEDs, term limits, and so on. Few companies link their board diversity policy to the business or strategic needs of the company.

Disclosure on director training is quite good, most issuers train all directors

The picture is similar for director training: one company achieved a high score but most scored 3. All companies provide some level of training for their directors and most do so for inside as well as independent directors. Training is largely of the ongoing variety (ie, post-appointment), although a few offer induction courses for new directors. Almost all issuers disclosed the content of courses in some detail, as required by regulation. Points were lost on this question, however, because most companies do not provide induction training and none organise site visits or field trips for their independent directors. The level of detail provided on course content is also sometimes a bit superficial.

Companies provide quite good narrative on board evaluation, as required by TWSE regulation

Somewhat better narrative is given on board evaluations, which scored an average of 3.5 out of 5. As per TWSE regulatory guidelines, companies conduct annual evaluations and engage a third-party consultant once every three years (helpfully the name of the consultant is usually provided). Information about evaluation methods and results are included, as required, although many companies only offer high-level, qualitative conclusions: board committees "operate well, and have a good grasp of the goals and tasks of the company and committee". Few list specific areas for improvement and next steps, neither of which is required by the regulations.

Where Taiwan performs averagely (2.5 out of 5)

Disclosure of individual director pay is getting better, but still some way from best practice

On individual director remuneration we are looking for figures outlining the exact remuneration of each director and at least the top five key management personnel by name, with pay broken down into key components (ie, salary, bonuses, pensions, stock awards, director fees, expenses, and so on). Rules have improved in this area in Taiwan in recent years and we note that two companies gained full marks, which helped to push the average score to 2.5/5. All other companies scored a 2. Unfortunately, the rules leave much to be desired, since companies have an option to disclose exact pay or in "bands" (ie, salary or fee ranges). Almost all opt for the latter. They also provide aggregate figures, which are only partially helpful, for the total pay of all executive/inside directors and all independent directors.

It should be noted that TWSE's "Regulations Governing Information to be Published in Annual Reports of Public Companies" (Article 10) requires several categories of underperforming companies to publish the exact remuneration of directors. For example, those which have posted after-tax deficits in any of the three most recent financial years. This list was expanded in November 2023. While expanding the scope of such reporting is a positive, it does not affect larger and mid-sized issuers which are performing well and of most interest to institutional investors.

Figure 24

Taiwan listed companies scores, CG Watch 2023

	Question	Average score	Range of scores
1.	Does the company's board governance reporting compare favourably against international best practice?	2	0.5-3
2.	How would you rate the quality of the company's ESG/sustainability reporting?	4.5	3-5
3.	Does the company provide comprehensive, timely and quick access to information for investors?	4	3-5
4.	Does the company undertake annual board evaluations, either internally or using external consultants?	3.5	2-5
5.	Does the company disclose and implement a credible board diversity policy?	3	0.5-5
6.	Does the company provide induction and/or ongoing training to all directors?	3	1-4
7.	Does the company have an independent chairman and/or a lead or senior independent director?	0	0-0
8.	Does the company disclose total remuneration of each member of the board of directors?	2.5	2-5
9.	Are the independent directors paid partly or wholly in stock options or restricted share awards? Do they share in a percentage of company earnings or other commissions in addition to their base fee?	4	1-5
10.	Are audit committees (or an equivalent) independently led and competent in financial reporting/ accounting matters?	4	3-5
11.	Does the company have an internal audit department that reports to the audit committee?	4	3-5
12.	Does the company provide a detailed explanation of its executive remuneration policies?	2	1.5-2.5
13.	Does the company have a nomination committee and is it independently led?	1.5	0-5
14.	Does the nomination committee have a female chair or at least one female director?	0.5	0-2

Source: ACGA research. Based on 15 large caps from a range of sectors

Where Taiwan performs poorly (0 to 2 out of 5)

Shallow CG reporting is a continuing feature of the corporate landscape . . .

Perhaps the most disappointing part of this entire survey for this author is the low average score of 2 out of 5 for CG reporting. As Figure 24 shows, the range of scores is even more depressing: from a low of 0.5 to 3. Indeed, only two firms scored 3. This question looks at the breadth and depth of disclosure on what boards and their committees discuss and decide each year, who the directors are and why they are on the board, and the effort made to inform shareholders and other stakeholders about board governance. We are looking for information specific to the company and the year in question that will help investors better understand the company's governance culture. Sadly, most companies report in a highly formulaic and abstract way, showing little creativity or improvement from previous surveys. They report what they must and little more. Clearly, they are under no pressure from the market to do more - which is also disappointing. Meanwhile, the contrast with the increasingly sophisticated and detailed sustainability reporting one finds is stark. (We hasten to add that we would say the same of all 12 markets in our survey, including Australia.)

. . . as is executive remuneration policy disclosure

Disclosure of executive remuneration policies is not much better. We are looking for plans that have clear objectives and KPIs over both the short- and long-term. Ideally, these should now be linked to climate/ESG outcomes as well as financial performance. Any options granted should not be subject to repricing. Plans should include a clawback in case of poor performance. And independent directors should be involved in developing remuneration policy. Unfortunately, most companies surveyed provide only general, high-level descriptions of their remuneration policies. KPIs are either not provided or only in qualitative terms. Few firms link remuneration to ESG outcomes. Three companies scored 2.5/5, while the remainder earned 2 or less.

Few companies have nomination committees, even though they are recommended

Despite being encouraged by the CG Best Practice Principles to have nomination committees since 2004, and then more firmly "advised" in 2020, few in our survey have them. Of the 15 companies surveyed, only six have standalone nomination or combined nomination/remuneration committees - and only two of these were in

existence before 2020. Although the CG Best Practice Principles explicitly call for such committees to have an independent chair and a majority of independent members, at least two of the six companies had insiders as chairs, while one more did not divulge who the chair was. Most meet only one to two times per year, which is not sufficient in our view. This paucity of nomination committees may be due to the legal-entity director issue in Taiwan: since corporate shareholders are entitled to nominate representatives to boards, and change them at will, what is the point of a nomination committee?

At least a few companies have female directors on their nomination committee

In terms of gender diversity, three of the six companies with nomination committees have one female director each on them - a small sign of progress at least. None have women chairing the committee. In other ACGA research around the region, such as in China and Hong Kong, we have found a broadly positive correlation between the presence of a female chair and more women directors on the board.

Taiwan is out of step on lead independent directors

Lastly, as in previous surveys, we found no company with an independent chair or lead independent director. The former is not surprising given the nature of corporate ownership in Taiwan, dominated as it is by family firms and state enterprises. However, the lack of lead independent directors reflects an area where Taiwan is out of alignment with regional best practice.

5. Investors

Taiwan improved to 6th on a slightly higher score of 40%

This category continues to be Taiwan's lowest scoring area, as it is for almost all markets, reflecting the nascent state of institutional investor stewardship and activism. Although overall we see a rising trend of stewardship by domestic investors and more informative stewardship reports, Taiwan's score only improved two percentage points to 40% because it also lost points in certain areas. Nevertheless, the higher score was enough to boost its ranking one place to 6th in 2023, helped by Thailand losing points and falling from equal 7th with Taiwan in 2020 to 8th. Singapore's score, meanwhile, remained the same at 39% and it moved down to 7th.

Institutional stewardship rising

Investors are becoming more active stewards

The understanding of investor stewardship is steadily developing in Taiwan. Asset managers publish more detailed stewardship reports. Engagement with individual listed companies is broadening. Disclosure of voting down to the company and resolution level is starting. And there is evidence that managers are more conscious today of conflicts of interest.

A dedicated page on the SITCA and TWSE websites makes tracking stewardship much easier today

One big leap forward in disclosure in recent years - and something that makes research in this area considerably more efficient - is the "Stewardship" page on the website of SITCA, the Securities Investment Trust & Consulting Association. It contains a helpful table listing 50 large asset managers, with links to their annual stewardship reports (dating back to 2019 for some managers), voting records, voting policies, "negotiation records" (where funds share engagement information), and statements on their compliance with the Taiwan Institutional Investor Stewardship Principles. This page is replicated on the TWSE CG Center website and includes exchange commentary on progress in investor disclosure since 2020, suggestions for further improvements in disclosure, seminars on best practice cases, and a list of the most transparent asset managers and examples of their disclosure on different aspects of stewardship. (Note: The top 50 list above contains both domestic and foreign-owned managers.)

All asset managers have proxy voting and CG policies, and publish stewardship reports . . . but are less transparent about resources allocated

All the managers listed on the SITCA website have proxy voting and CG/sustainability policies, with some of the disclosure being of a high standard. Generally, asset managers provide more useful information in this regard than local asset owners. All owners and managers have signed the Stewardship Principles and publish reports on their activities. Less impressive is transparency around the staffing and financial resources that funds apply to stewardship (anecdotally, this seems to be limited) and the extent to which they get involved in public consultations on CG reform (almost no public comment, but some involvement in private "soft" discussions). For all these reasons and considering how Taiwan compares to markets that have more advanced stewardship regimes, such as Japan, we left the score at 3 out of 5.

Investors share information about company engagement

To what extent are institutional investors engaging directly with listed companies on topical CG or ESG issues? Most asset managers say something about this in their stewardship reports and use the dedicated "negotiation" tab on the SITCA website to share information. Again, very few share information on how many people are in their engagement team or what level of skills they possess. There is little evidence of collective engagement. A review of some reports indicates local investors are having real conversations on specific topics with their investee companies. Our score rose slightly here to 2.5 out of 5.

Disclosure of voting to the company level is new . . . and not yet common

One new area of disclosure is reporting on voting down to the company and resolution level. While not mandatory, the Stewardship Principles encourage it. We surveyed the top nine asset managers on this point and found that while all disclose general data on their voting, only four disclosed to the company/resolution level while against votes were not explained. We raised our score from zero to 1 out of 5 for investors making a start in this area.

Disclosure on conflicts of interest is improving from a very low base

Conflicts of interest is another area that earned zero points in CG Watch 2020. At the time we found that while all funds had a policy of some sort on this, almost none said anything of substance about it in their disclosure. We also felt that most missed the point, laying responsibility at the employee not corporate level. Since that time, regulators have put much more emphasis on this issue and investors are responding: some leading asset owners have detailed and well-developed policies, while the record of asset managers is more mixed. Not many funds have credible explanations as to how they manage conflicts. We gave a point for making a start.

At last, an activist

Taiwan got its first real activist funds in 2023 . . .

In contrast to markets like Japan and Korea, genuine institutional shareholder activists that engage with companies over a multi-year period to improve governance and corporate value have been rare in Taiwan. There are likely many reasons for this: better, easier or more opportunities elsewhere; the nature of corporate ownership, where families or the state dominate; and the absence of domestic demand for homegrown funds with an explicit CG/corporate value focus.

. . . with a shareholder proposal from TIH and Argyle St at the Catcher AGM

This is no longer the case with the arrival of Singapore-listed TIH Limited and Hong Kong-based Argyle Street Management in April 2023 and their campaign against Catcher Technology, a large electronic casings firm. The pair submitted a shareholder proposal to amend the articles of Catcher so that its huge cash reserves could be distributed as dividends. The board of Catcher, controlled by three brothers of the Hung family, refused to include the proposal in its AGM agenda on technical grounds. It argued that the resolution touched on two items, rather than one, which would render it foul of Taiwan's Company Act.

Shareholders angry that Catcher refused to include the proposal in the agenda

The move subsequently drew investor ire at Catcher's 2023 AGM. Four investors stood up against the board chairman Hung Shui-shu, including Argyle Street, TIH, and the SFIPC. Notably, the SFIPC voiced the view that the resolution "should be considered as one single proposal".

Catcher sued the activists, the SFB fined Catcher's chairman, now TIH and Argyle are back

Catcher, however, stood its ground. In June 2023, it filed a defamation suit against Allen Wang, the Taiwanese CEO of TIH, accusing him of creating and spreading false information about the company on dedicated websites. But in August 2023, the SFB sided with the investors and issued a NT$240,000 (US$7,500) fine to Hung Shui-shui for a "clear" violation of the Company Act. In April 2024, the same proposal filed by TIH and Argyle Street was finally included on the agenda of Catcher's 2024 AGM. In recognition of the efforts of TIH and Argyle Street, we added a point on this question, bringing Taiwan's score to 1 out of 5.

The retail dimension

Retail investors can be quite vocal in AGMs

We also raised scores slightly for two questions relating to retail investors (Q5.14 and Q5.16): whether they are actively asking questions in AGMs and whether they are launching any activist campaigns against errant directors or companies. Companies where small shareholders posed questions in recent years include Nanshan Life Insurance, where employees and union members who were also shareholders raised pointed questions of Yin Chung-yao, son of Ruentex Group President Samuel Yin Yen-liang, at the company's AGM in June 2023. Yin was chairing his first annual meeting and allowed questions to go on for the best part of three hours. Retail shareholders also asked questions at the AGMs of China Development Financial and Foxconn, among others, during 2023.

There is even some retail activism

As for retail activism, Taiwan annual meetings during 2023 attracted the usual range of colourful participants. One of the more successful ones went by the nickname of "Old Naughty Boy" and through an internet campaign managed to get himself elected to the board of Grand Pacific Petrochemical. He was primarily upset about the company's dividend policy. Despite having a professional background in education - he is CEO of two private high schools and chairman of a digital distance learning platform - he was far and away the preferred candidate among regular (ie, non-independent) directors. Other companies subject to various forms of retail action included Taipower, Starlux, and Chung Fu Tex.

Challenges

Foreign investor involvement in CG in Taiwan is limited

Against progress being made by domestic institutional investors in stewardship and increased pressure from retail shareholders, scores declined in a few areas in this category, thus holding down the overall total. These mostly related to the involvement by foreign institutional investors in Taiwan's CG environment. Although many foreign investors have CG policies relevant to Taiwan, are signatories to the Stewardship Principles, and vote against management resolutions, we deducted a point on the latter issue due to a generally lower level of targeted voting and less informative disclosure on voting records compared to other markets, principally Japan. Taiwan's score here (Q5.4) fell a point to a still respectable 4 out of 5.

Little evidence of foreign investors attending AGMs

We lowered our rating on whether foreign investors attend AGMs in person (Q5.6). It fell from a low 1 out of 5 to zero, as we could not find evidence of this during 2023. Admittedly, physical attendance was not possible during Covid, but travel resumed in 2023 and quite a few foreign investors travelled to other parts of Asia to attend meetings.

Domestic asset owners are not yet showing the leadership in stewardship of their counterparts in other parts of Asia

We also cut scores on two questions relating to domestic institutional investors. The first (Q5.3) relates to whether most domestic institutions exercise their voting rights and actively vote against resolutions with which they disagree. Of the nine major asset managers we reviewed, all exercise their rights and disclose how they vote. Yet six generally do not vote against any resolutions. The other question that lost points asks if domestic asset owners are playing a leadership role in corporate governance and stewardship in Taiwan (Q5.8). While there are promising signs of this emerging in the near term, we reassessed our previous score of 2/5 and concluded that it was too early to give points at this stage compared to the strong leadership and proactive efforts of certain state pension and investments funds in other markets in the region. We therefore cut the score to zero.

SFIPC can now issue press releases before AGMs on issues of concern

SFIPC gains new powers to monitor AGMs

One of the most unique aspects of Taiwan's shareholder meeting environment is the role played by the Securities and Futures Investors Protection Center (SFIPC) in these events. As a shareholder in its own right, the Center has been attending AGMs since at least 2012 (see Figure 25). It then further enhanced its measures for monitoring meetings in June 2022, including issuing press releases beforehand about areas of concern and afterwards if it feels it has more to say. It partly selects the companies to focus on based on those that scored poorly within their sectors in the annual Corporate Governance Evaluation by the TWSE. It also decides on the basis of how companies respond to queries it raises in letters sent before AGMs. If issuers respond satisfactorily, the SFIPC will not attend. If they do not, then it will go.

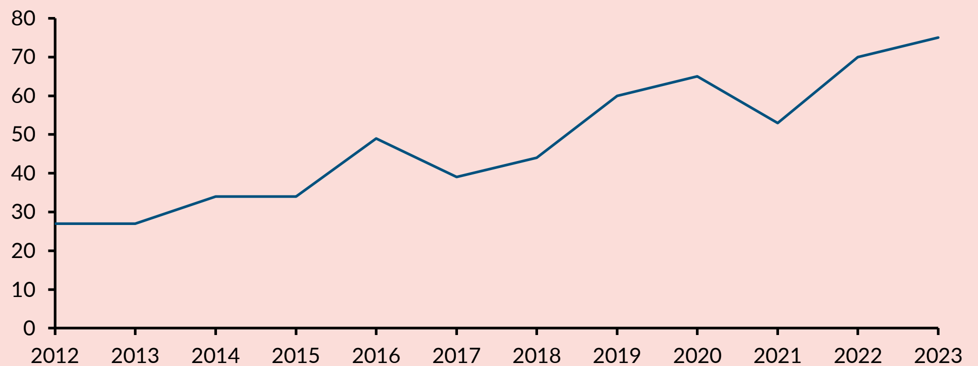
It attended 75 annual meetings in 2023 . . .

The Center is open about the meetings it attends each year and publishes tables with dates, names, and specific issues of concern. In 2023 it attended 75 meetings, one of which was the Catcher AGM on 30 May 2023 when the company refused to include in the AGM agenda a proposal from Pagoda Street and Vasanta Master Fund (managed by Argyle Street and TIH respectively) to amend its Articles regarding how dividends were decided. In several cases, such as Cathay Holdings, Yuanta Group, China Motor Company, and a number of smaller issuers, it primarily wanted to observe the way in which these companies organised their meetings via online communication platforms. (For details see the following URL: https://www.sfipc.org.tw/MainWeb/Article.aspx?L=2&SNO=rmZaArXNn9Y4a364yNEwJg==)

. . . compared to less than 30 in 2012

Figure 25

SFIPC AGM attendance status, 2012 to 2023 (number of meetings)



Source: ACGA

6. Auditors & audit regulators

Taiwan leapt from equal 6th to equal 2nd on a much-improved score of 83%

This was Taiwan's best performing category, with both its score rising seven percentage points to 83% and its ranking jumping from equal 6th to equal 2nd with Singapore and Japan. Audit regulation has been a significant area of focus in recent years and scores increased on seven of the 10 questions in this category. They only fell on one.

Audit quality indicators

Taiwan has joined the AQI bandwagon

The headline change since our last survey has been the introduction of a system of "audit quality indicators" (AQIs), a concept first adopted in the region by Singapore in 2015. The Taiwan version was announced in November 2021 and took effect in 2023 for the Big Four accounting firms and 2024 for non-Big Four. More specifically, Big Four firms needed to start gathering data from Q4 2022 and fill in a detailed template to help their clients appoint auditors for their 2023 financial report.

Taiwan's version is extensive and covers 13 quality indicators

The program covers 13 indicators across 5 "dimensions" that include "profession", "quality control", "independence", "monitoring", and "innovation". The first dimension, for example, focusses on audit experience, training hours, attrition rate, and professional support (eg, experts able to use computer-aided audit tools, financial appraisers, and so on). The AQI Disclosure Template then sets down the information requirements for each AQI. Under audit experience, for example, firms must provide data on years of experience of audit partners, engagement quality control reviewers, and audit managers or above (excluding partners). This must be provided for both the firm overall and individual audit engagements. A description of the educational and professional background of engagement team members is also required. Detailed information is required for the other four dimensions too, including having to report under "monitoring" on previous years' inspection results by the FSC, PCAOB, and any CPA disciplinary sanctions applied to the firm. Moreover, firms must outline the number of "official improvement letters" (OILs) they have received at the firm and engagement level. All in all, it is an extensive regime and will no doubt provide some fascinating insights into the audit industry in Taiwan and the challenges it faces.

Big Four firms must publish transparency reports

Accompanying the AQI system is requirement for Big Four audit firms to publish transparency reports starting from 2023. This follows similar programmes in other parts of region, such as Australia, Singapore, Malaysia and Thailand, which have had such reports for several years. As the FSC explains, transparency reports "shall provide information that is fact-based, not potentially misleading and not oriented toward marketing or selling services". This is probably easier said than done, since transparency reports in other jurisdictions tend to be a combination of highly useful information and marketing filler. Apart from background on firm history, ownership structure and any network to which the firm belongs, the FSC says transparency reports should address such things as firm governance, information on audit quality (ie, a shortened version of the AQI Disclosure Template), a description of the firm's partner rotation policy and other relevant information. These reports must be put on the firm's website and made available for five years.

While these efforts are impressive, they are still new. We therefore increased the score on the related question (Q6.10) by half a point to 3.5 out of 5.

Audit regulation

Disclosure of enforcement action is improving . . .

Scores increased also for the quality of disclosure on disciplinary action and CPA firm inspections by the audit oversight board, the Accounting and Auditing Supervision Division under the Securities and Futures Bureau (SFB). One general comment is that the Division's annual report these days is longer, more detailed and more useful than in previous years. While the enforcement section is somewhat brief, it refers to a page on the SFB website that provides links to enforcement action against individual CPAs for each year going back to 2018. Each case is translated into English, is informative, and updated quickly. There is also a link to a spreadsheet summarising all these cases from 2018. We duly added a point to our question (Q6.8), taking the score to 3 out of 5. It is hard to give more points, however, because enforcement data is still presented in a rather fragmentary way and hard to find on the SFB website.

. . . as is disclosure of regulatory inspections of CPA firms

We also added a point for the Division's disclosure of its annual inspection work. Its 2019 report (published June 2020) ran to 38 pages but devoted only about five pages to inspections. The 2021 report (published July 2022) increased marginally to 42 pages but the section on inspections was about three times larger (16 pages) and significantly more detailed about both firm-level quality control issues and audit engagement deficiencies. It also compared Big Four firms to non-Big Four in this area: as expected, absolute levels of deficiencies were noticeably lower, but the big firms still shared some of the same problems. These improvements took the score to 4 out of 5 for Q6.9.

We slightly cut the score for the powers of the regulator

The one question where scoring fell related to the powers of the audit regulator. The FSC/SFB has broad authority over auditor registration (delegated to the CPA Association), inspection, investigation (sometimes delegated to the TWSE), sanction, and standard setting (delegated to ARDF, but subject to FSC approval). Yet there is a view that its penalty options are blunt and often too tough. What it needs is a wider range of sanctions and penalties that could be applied depending on the severity of the crime. We reduced the score slightly by half a point to 4.5 out of 5 for Q6.6.

Audit and non-audit fees

Taiwan now requires full transparency on audit and non-audit fees

Taiwan has finally earned full marks in our survey for the disclosure of audit and non-audit fees. Previously this information could be disclosed in bands and non-audit fees were only disclosed if they were more than 25% of audit fees. Today the exact amount of fees must be disclosed for each, as well as details on any non-audit services.

Taiwan has a unique rule whenever audit fees fall by 10% or more

It is also worth noting that Taiwan has a rather unique rule that kicks in when audit fees drop by 10% or more: the amount and reasons for the change must be disclosed. The rule states: "When the audit fees paid for the current fiscal year are lower than those for the previous fiscal year by 10 percent or more, the reduction in the amount of audit fees, reduction percentage, and reason(s) therefor shall be disclosed." We would like to see similar rules adopted in other markets, since experience suggests that lower audit fees rarely lead to higher audit quality.

7. Civil society & media

Taiwan slipped to 5th on the same score of 62%

Despite a thriving civil society, Taiwan slipped in ranking from equal 4th with Japan in 2020 to 5th in 2023. Its score remained the same at 62%. Japan, in contrast, increased in score several percentage points and moved up to 3rd. Scores increased on four questions and fell on four. We are seeing notable improvements in director training and the involvement of professional associations in promoting understanding of CG and ESG issues, as well as progress in original research by professional bodies and media skills. We also reassessed scores where evidence suggests that the strength of civil society in Taiwan is somewhat weaker than in other markets, warranting a reduction in points.

Director training

Director training in Taiwan is guided by a best-practice

As with most aspects of Taiwan's CG regime, director training takes place within a best practice framework devised by the regulator. The "Directions for the Implementation of Continuing Education for Directors and Supervisors of TWSE Listed and TPEx Listed Companies" were first issued in 2003 and amended many times since. It aligns with certain articles in the CG Best Practice Principles and "encourages" issuers to provide training to newly appointed directors (ie, those serving for the first time in a listed company) as well as re-appointed directors (including independent directors) and supervisors. The guidance advises a minimum of 12 hours training for new directors/supervisors in their first year and six hours thereafter. Reappointed directors/supervisors should do at least six hours. It also specifies a list of recognised institutions permitted to provide training.

Taiwan lacks a central IOD, but instead has numerous bodies providing training

Taiwan lacks the institutional model of a single, authoritative institute of directors serving the entire director universe as found in many other markets. It does however have an array of organisations providing training for directors and supervisors. According to the TWSE Corporate Governance Center, which devotes a section of its website to "Directors and supervisors training", there are 32 organisations authorised to provide continuing education. Courses cover a dizzying range of topics from basic corporate governance, sustainability, and risk management to GHG inventory verification, financial statement analysis, data governance, and audit reform. It is clear that many of these courses are for professionals, not just directors and supervisors.

TCGA is one of the more established training providers

One of the more established training providers is the Taiwan Corporate Governance Association (TCGA), established in March 2002 and recognised as Taiwan's leading CG non-profit. It offers foundational as well as advanced courses, including on specialised topics such as ESG and AI. TCGA also has an "Association of Directors and Supervisors" for more senior directors and offers a range of events designed specifically for this group.

Multi-day courses are on offer from several entities

The Securities and Futures Institute (SFI), a government-funded entity, provides training for new directors, including a multi-day, 12-hour course for newly appointed directors and corporate governance officers (who perform a similar role as company secretaries). Other multi-day programmes are arranged by the Accounting Research and Development Foundation (ARDF) and the Taiwan Law Foundation. ARDF also runs specific courses on the impact of carbon emissions on financial statements and corporate fraud in addition to standard courses on accounting and financial reporting.

TWIOD and TIDA serve different constituencies

Two other entities deserve a mention in this context: the Taiwan Institute of Directors (TWIOD), which despite its name is not an official body, and the Independent Directors Association Taiwan (TIDA). Formed only in 2012, TWIOD positions itself as a "think tank and advisor to corporate boards of directors" and works mainly in the family business space. Indeed, it was largely formed by scions of major family companies in Taiwan and fills a particular niche. It runs training courses for directors on significant CG and ESG subjects through its "Directors Academy" and puts on regular seminars for members on topical issues. TIDA is a younger organisation, created in 2018, and has been running both open courses for independent directors and in-house training for companies.

The score for training improved a point to 4/5

For these reasons, our score on director training (Q7.1) rose a point to 4 out of 5. We did not give a 5 because the fragmentation of the training system makes it somewhat hard to ascertain how effective and coordinated all this training is, whether there are clear course progressions from beginner to intermediate to advanced, and the number of directors and supervisors being trained each year.

Professional associations

Numerous professional bodies promote CG and ESG

As indicated, there is a diverse ecosystem of professional bodies and institutes involved in raising awareness of CG and ESG in Taiwan. There were more than 400 approved training events in sustainable development alone in 2023. In addition to the entities mentioned above, these other entities include the likes of the Computer Audit Association, which offers a course on fraudulent/false financial reports and forensic data analysis techniques; the Taipei Foundation of Finance, which provides an impressive array of courses, mostly focused on ESG topics; the Taiwan Investor Relations Institute, which teaches its members about ESG and shareholder activism, among other things; and the Commerce Development Research Institute that organises a 36-hour certificate class in AFNOR (French certification entity) Sustainability Strategy Management. Many professional bodies provide original reports and guidelines on CG and ESG topics for their members.

Lagging behind

The company secretary space in Taiwan is still emerging

One area where Taiwan lags the region is in the role of company secretaries, a situation being addressed to an extent by the new requirement for "corporate governance officers" in listed companies. This has led to some training being specifically designed for them by organisations such as SFI and ARDF. Meanwhile, an entity founded in 2018 to fill this professional gap, the Governance Professionals Institute of Taiwan, which became affiliated with ICSA of the UK (now called The Chartered Governance Institute), has been noticeably less active than in the past. We cut the score for the relevant question (Q7.2) by a point to 1 out of 5.

Taiwan still lacks an independent investor NGO dedicated to CG

We decided to reduce the score for a question (Q7.5) on the existence of non-profit organisations working to promote CG and ESG. Despite a rich ecosystem of NGOs, including some not mentioned yet (eg, the Business Council for Sustainable Development and the Taiwan Institute for Sustainable Energy), Taiwan still lacks a local institutional or retail investor advocacy group that is independently established (ie, without government grandfathering), funded from private (not public) sources, and dedicated to raising standards of CG. Since best practice in other markets is to have such a body (or bodies), we felt full marks on this question was objectively too generous and we cut a point for a score of 4 out of 5.

Public participation by NGOs in regulatory consultations is rare

Scores also fell for the extent to which civil society groups participate actively and publicly in regulatory consultations (Q7.6). They do, but mostly informally and at the behest of government. It is hard to find evidence of written submissions. We further cut half a point (Q7.4) for the contribution to CG promotion of business associations, such as the China National Association of Industry and Commerce, and investment industry bodies, namely the Securities Investment Trust & Consulting Association. While these entities do play a role, it is a rather limited one and less than their counterparts in markets such as Thailand and India.

Downgrade watchlist

What to avoid

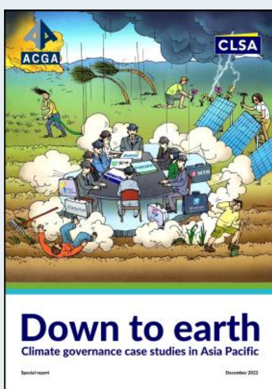
Factors that could force Taiwan's market score to fall in 2025:

- Any backtracking on the implementation schedule for sustainability/GHG reporting and GHG inventory assurance
- Lower enforcement outcomes and no improvement in the disclosure of the outcomes of individual criminal prosecutions
- No improvement in the public consultation process for new CG/ESG rules
- No improvement in regulations governing entrenched issues such as related-party transactions and legal-entity directors
- No improvement in corporate CG disclosure, including reporting on individual director and executive remuneration
- No revision of rules governing the content of virtual AGMs

Next Steps

Our recommendations for the next stage of CG reform in Taiwan include the following ideas. Our aim here is to suggest action points that are important, quite urgent, and capable of being implemented over the short to medium term:

Recommendations for the next phase of reform



1. **Sustainability governance**: Given the critical importance of Taiwan's commitment to sustainable development, sustainability reporting and assurance, we suggest there should be a structured and open discussion between key stakeholders (regulators, listed companies, investors, relevant NGOs) on the most sensible ways forward for companies to build stronger sustainability governance mechanisms. There is a risk that an overly prescriptive approach by government, such as mandating specific board committees or an independent director with specialised expertise, could lead to box-ticking without meaningful improvements in decision-making. ACGA's research in late 2022 (see *Down to Earth*) showed that companies require some flexibility in how they approach the governance of climate risks and opportunities. It is important for boards to have oversight of these decisions, but equally critical that they work effectively with management and have a sound framework for doing so. Different companies have created different organisational structures to manage this process and there is no consensus yet on what is best practice. Developing the right level of skills internally will also be critical, as will communicating plans and targets effectively to shareholders and stakeholders. Government does not have all the answers here.

2. **Public consultations:** Following from the above, it would be helpful if government and regulators undertook more consultation, both "soft" (private) and "hard" (public), before finalising new CG rules. More detailed consultation papers that outline not only the new rules, but the regulatory rationale for these rules, would help. So would longer response periods, the publication of all submissions, and systematic communication with foreign investors.

3. **Corporate governance disclosure:** Despite some genuine improvements in board operations and oversight over the past decade, too many companies continue to follow the rulebook to the letter and disclose only what is required. At best this produces activity "lists" that are somewhat informative but lack context and accompanying narrative. At worst it produces boilerplate text that reads the same from one company to the next. Motivating companies to move away from such reporting is challenging, since no one wants to be the first and companies often rely on IR/PR consultants who use the jargon of the day. An independent survey of listed companies and their shareholders could well provide useful insights as to the root causes of this problem and practical ways forward. At this stage, more guidance or regulation is unlikely to be received with enthusiasm by issuers. Peer-group comparisons with overseas competitors might also move the needle.

4. **Regulatory websites:** It would be helpful for key regulators to benchmark their websites against counterparts in other markets, especially in the organisation of information on key laws and regulations, enforcement statistics and announcements, and annual budgets.

5. **Criminal prosecution outcomes:** While the remit of financial regulators does not extend to undertaking criminal prosecutions and imposing criminal fines or imprisonment, it would be helpful if the outcomes of individual cases referred by the FSC/SFB for criminal investigation and prosecution were systematically reported on their website and that of MJIB. This would provide a more complete picture of enforcement efforts in Taiwan.

6. **Nomination committees:** For a range of reasons, partly due to the presence of legal-entity directors, nomination committees have yet to become the norm in Taiwan. These committees play a powerful coordinating role across many aspects of board governance today, including developing skill matrices and board diversity policies, managing board evaluations and training, and building a pipeline of potential director candidates. Even if legal-entity directors are selected by major shareholders and removed at will without any input from the board or shareholders, there remains a value for an effective and skilled nomination committee. This concept needs further socialisation.

7. **Lead independent directors:** In the absence of an independent director chairing board meetings, it would be beneficial to amend regulations to create a "lead independent director" position. Such a director not only provides balance in board discussions (which could otherwise be dominated by the chairman) but is expected to lead discussion among other independent or outside directors in the absence of management and be a principal point of contact for institutional shareholders.

8. **Investor stewardship:** There is scope in Taiwan for asset managers to do more in this area, including disclosing voting down to the company and resolution level, undertaking collective engagement where appropriate (both among domestic managers and with foreign investors), and for asset owners to play a leadership role in setting the governance and sustainability agenda. Institutional investors could also be a more vocal presence at AGMs.

Company checklist

Actions that Taiwan companies could take over the short to medium term to enhance their governance practices and disclosure include the following:

Actions companies could take to enhance CG practice and disclosure immediately

1. **Composition/structure:** Benchmark board composition, structure and disclosure against global peers and local best practices.

2. **Board reporting:** Ensure reporting on board and board committee activities is meaningful. It should contain sufficient narrative for a reasonable investor to understand what the board and its committees have done during the year, how both inside and outside directors/auditors have contributed, and what the key points of discussion and decisions have been. Disclosure should be specific to the company, not generic, and focus on the year in question. There should also be meaningful narrative on the relationship between internal audit and the audit committee or independent directors.

3. **Nomination committee**: Appoint a nomination committee with an independent chair and at least one female director. ACGA research has found that having women directors on a nomination committee typically leads to a higher proportion of women on boards.

4. **Board diversity policy**: Ensure any policy is meaningful, not generic, and contains sensible targets and action plans. Link targets to the strategic needs of the company, rather than simply copying regulatory guidance.

5. **Director training:** Ensure there is room in the director training budget for induction as well as continuing training for newly appointed directors and even experienced directors who are new to the company. Organise site visits so that independent directors become more familiar with the company's wider operations.

6. **Board evaluations:** While the evaluation process is well-explained by most companies, as required by regulation, there is limited disclosure of results beyond scores achieved (which are always high). Provide some narrative on the findings of the evaluation, in qualitative terms, and outline action points for improvement. A brief couple of paragraphs summarising such evaluations are rarely of benefit to investors.

7. **Director/executive remuneration disclosure:** Follow global/regional best practice and disclose the exact remuneration for each director by name, broken down into constituent parts, and at least the top five key management personnel. This should apply to all listed companies, starting with the larger ones, not just those which have been underperforming.

Click to rate this research

Great

Solid

Meh

Companies mentioned

1947 Trustee Limited (N-R)
3 Group Europe (N-R)
AIA (1299 HK - HK$52.50 - O-PF)[1]
Alibaba (BABA US - US$78.62 - O-PF)[1]
Argyle Street Management (N-R)
ASE (3711 TT - NT$153.5 - U-PF)[2]
Baidu (BIDU US - US$88.98 - O-PF)[1]
BDO (N-R)
BlackRock (N-R)
BNP Asset Management (N-R)
Catcher Tech (N-R)
Cathay Holdings (N-R)
China Candy Holdings (N-R)
China Clean Energy Technology Group (N-R)
China Development (N-R)
China Evergrande (N-R)
China Fortune Holdings (N-R)
China Gem Holdings (N-R)
China Longevity (N-R)
China Mobile (941 HK - HK$73.20 - O-PF)[1]
China Motor Company (N-R)
Chung Fu Tex (N-R)
CPIC (2601 HK - HK$19.56 - HLD)[1]
DeHeng Law Offices (N-R)
Deloitte (N-R)
Ernst & Young (N-R)
Essence Information Technology (N-R)
Facebook (N-R)
Fidelity (N-R)
First Pacific (142 HK - HK$3.36 - O-PF)
Foxconn (N-R)
Grand Pacific Petro (N-R)
Grandall Law Firm (N-R)
Guangdong Zhengzhong Pearl River Accounting Firm (N-R)
HK Exchanges (388 HK - HK$231.00 - O-PF)[1]
HK Resources (N-R)
HLB Hodgson Impey Cheng (N-R)
HSBC (5 HK - HK$67.30 - N-R)
Huarong Asset Mgmt (2799 HK - HK$0.37 - N-R)
JD.com (JD US - US$26.61 - O-PF)[1]
Jilin Province Huinan Changlong Bio-pharmacy Company (N-R)
JP Morgan (N-R)
Kangmei Pharma (N-R)
King & Wood Mallesons (N-R)
KPMG (N-R)
Kweichow Moutai (600519 CH - RMB1,398.02 - O-PF)[1]
Le.com (N-R)
LGIM (N-R)
Li Auto (LI US - US$19.14 - O-PF)[1]
Liaoning SG Automotive (N-R)
Long Bon (N-R)
Meituan (3690 HK - HK$108.40 - O-PF)[1]
MTR (66 HK - HK$25.25 - O-PF)[1]
Nanshan Life Insurance (N-R)
Netac Technology (N-R)
NetEase (NTES US - US$91.18 - O-PF)[1]
Pagoda Street (N-R)
Pharmally (N-R)
PICC Group (1339 HK - HK$2.56 - O-PF)[1]
Ping An - A (601318 CH - RMB41.32 - O-PF)[1]
Ping An (2318 HK - HK$33.70 - O-PF)[1]
PWC (N-R)
Ruentex Group (N-R)
S&S Intervalue China (N-R)
Shandong Haoxin (N-R)
Shanghai Yingyi Investment Center (N-R)
Silicon Precisionware Industries (N-R)
Sound Global (N-R)
Starlux (N-R)
Sun Cheong Creative Development (N-R)
SynTao Green Finance (N-R)
Taipei Exchange (N-R)
Taiping Insurance (966 HK - HK$7.76 - O-PF)[1]
Taipower (N-R)
Taisun (N-R)
Taiwan Futures Exchange Corporation (N-R)
TIH Limited (N-R)
Trip.com (TCOM US - US$43.09 - O-PF)[1]
TVB (N-R)
TWSE (N-R)
Universal Star (Holdings) (N-R)
Vasanta Master Fund (N-R)
Weibo (WB US - US$7.69 - HLD)[1]
Wuxi Apptec - A (603259 CH - RMB39.00 - O-PF)[1]
WuXi AppTec (2359 HK - HK$28.75 - O-PF)[1]
Xiaomi (1810 HK - HK$16.82 - O-PF)[1]
Yuanta Group (N-R)
ZD CPA (N-R)
ZD Proxy Shareholder Services (N-R)
Zhejiang Expway (N-R)

[1] Covered by CLSA; [2] Covered by CLST

Analyst certification

The analyst(s) of this report hereby certify that the views expressed in this research report accurately reflect my/our own personal views about the securities and/or the issuers and that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation or views contained in this research report.

Important disclosures

CLSA ("CLSA") in this report refers to CLSA Limited, CLSA Americas, LLC, CLSA Australia Pty Ltd, CLSA India Private Limited, PT CLSA Sekuritas Indonesia, CLSA Securities Japan Co., Ltd., CLSA Securities Korea Ltd., CLSA Securities Malaysia Sdn. Bhd., CLSA Philippines, Inc, CLSA Singapore Pte Ltd, CLSA Securities (Thailand) Limited, CLSA (UK), CLSA Europe B.V. and/or their respective affiliates. CLST ("CLST") in this report refers to CL Securities Taiwan Co., Ltd.

The policies of CLSA and CLST are to only publish research that is impartial, independent, clear, fair, and not misleading. Regulations or market practice of some jurisdictions/markets prescribe certain disclosures to be made for certain actual, potential or perceived conflicts of interests relating to a research report as below. This research disclosure should be read in conjunction with the research disclaimer as set out hereof and at www.clsa.com/disclaimer.html, the Terms and Conditions of Use as set out at https://www.clsa.com/terms-and-conditions-of-use/ and the applicable regulation of the concerned market where the analyst is stationed and hence subject to. Investors are strongly encouraged to review this disclaimer before investing.

Neither analysts nor their household members or associates may have a financial interest in, or be an officer, director or advisory board member of companies covered by the analyst unless disclosed herein. In circumstances where an analyst has a pre-existing holding in any securities under coverage, those holdings are grandfathered and the analyst is prohibited from trading such securities.

The analysts included herein hereby confirm that they have not been placed under any undue influence, intervention or pressure by any person/s in compiling this research report. In addition, the analysts attest that they were not in possession of any material, non-public information regarding the subject company that has securities listed in the relevant jurisdiction(s) at the time of publication of this report. (For full disclosure of interest for all companies covered by CLSA in this report, please refer to http://www.clsa.com/member/research_disclosures/ for details.)

As analyst(s) of this report, I/we hereby certify that the views expressed in this research report accurately reflect my/our own personal views about the securities and/or the issuers and that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation or views contained in this report or to any investment banking relationship with the subject company covered in this report (for the past one year) or otherwise any other relationship with such company which leads to receipt of fees from the company except in ordinary course of business of the company. The analyst/s also state/s and confirm/s that he/she/they has/have not been placed under any undue influence, intervention or pressure by any person/s in compiling this research report. In addition, the analysts included herein attest that they were not in possession of any material, non-public information regarding the subject company that has securities listed in the relevant jurisdiction(s) at the time of publication of this report. The analysts further confirm that none of the information used in this report was received from CLSA's Corporate Finance department or CLSA's and/or CLST's Sales and Trading business. Save from the disclosure below (if any), the analyst(s) is/are not aware of any material conflict of interest.

Key to CLSA/CLST investment rankings: From 6pm (HK time) on 28 June 2024: Outperform (O-PF): Total stock return (TSR) expected to exceed or be equal to 10%; Hold (HLD): Total stock return expected to be below 10% but more than or equal to negative 10%; Underperform (U-PF): Total stock return expected to be below negative 10%. TSR is up/downside to 12-month target price plus dividend. Up to 6pm (HK time) on 28 June 2024: BUY: Total stock return (including dividends) expected to exceed 20%; O-PF (aka ACCUMULATE): Total expected return below 20% but exceeding market return; U-PF (aka REDUCE): Total expected return positive but below market return; SELL: Total return expected to be negative. For relative performance, we benchmark the 12-month total forecast return (including dividends) for the stock against the 12-month forecast return (including dividends) for the market on which the stock trades.

"High Conviction" Ideas are not necessarily stocks with the most upside/downside, but those where the Research Head/Strategist believes there is the highest likelihood of positive/negative returns. The list for each market is monitored weekly.

According to the key to CLSA/CLST investment rankings effective from 6pm (HK time) on 28 June 2024: Overall rating distribution for CLSA (exclude CLST) only Universe: Outperform - CLSA: 72.61%, Hold - CLSA: 18.39%, Underperform - CLSA: 9.00%, Restricted - CLSA: 0.39%; Data as of 28 June 2024. Investment banking clients as a % of rating category: Outperform - CLSA: 14.60%, Hold - CLSA: 1.03%, Underperform - CLSA: 1.03%; Restricted - CLSA: 0.39%. Data for 12-month period ending 28 June 2024. Overall rating distribution for CLST only Universe: Outperform - CLST: 79.66%, Hold - CLST: 8.47 %, Underperform - CLST: 11.86%, Restricted - CLST: 0.00%. Data as of 28 June 2024. Investment banking clients as a % of rating category: Outperform - CLST: 0.00%, Hold - CLST: 0.00%, Underperform - CLST: 0.00%, Restricted - CLST: 0.00%. Data for 12-month period ending 28 June 2024. For purposes of regulatory disclosure only, our Outperform rating falls into a buy rating category; our Hold rating falls into a hold rating category; and our Underperform rating falls into a sell rating category.

According to the key to CLSA/CLST investment rankings effective up to 6pm (HK time) on 28 June 2024: Overall rating distribution for CLSA (exclude CLST) only Universe: BUY / Outperform - CLSA: 72.61%, Underperform / SELL - CLSA: 27.39%, Restricted - CLSA: 0.39%; Data as of 28 June 2024. Investment banking clients as a % of rating category: BUY / Outperform - CLSA: 14.60%, Underperform / SELL - CLSA: 2.05%; Restricted - CLSA: 0.39%. Data for 12-month period ending 28 June 2024. Overall rating distribution for CLST only Universe: BUY / Outperform - CLST: 79.66%, Underperform / SELL - CLST: 20.34%, Restricted - CLST: 0.00%. Data as of 28 June 2024. Investment banking clients as a % of rating category: BUY / Outperform - CLST: 0.00%, Underperform / SELL - CLST: 0.00%, Restricted - CLST: 0.00%. Data for 12-month period ending 28 June 2024. There are no numbers for Hold/Neutral as CLSA/CLST do not have such investment rankings.

For a history of the recommendation, price targets and disclosure information for companies mentioned in this report please write to: CLSA Group Compliance, 18/F, One Pacific Place, 88 Queensway, Hong Kong and/or; CLST Compliance (27/F, 95, Section 2 Dun Hua South Road, Taipei 10682, Taiwan, telephone (886) 2 2326 8188). EVA® is a registered trademark of Stern, Stewart & Co. "CL" in charts and tables stands for CLSA estimates, "CT" stands for CLST estimates, "CRR" stands for CRR Research estimates and "CS" for CITIC Securities estimates unless otherwise noted in the source.

Charts and tables sourced to CLSA in this report may include data extracted from CLSA's automated databases, which derive their original data from a range of sources. These can include: companies; analyst estimates/calculations; local exchanges and/or third-party data or market pricing providers such as Bloomberg, FactSet or IBES. Additional information on data sources for specific charts or tables can be obtained by contacting the publishing analysts.

This report is subject to and incorporates the terms and conditions of use set out on the www.clsa.com website (https://www.clsa.com/disclaimer.html and https://www.clsa.com/terms -and-conditions-of use/) and the references to "publication/communication" or "Publications" thereof shall include this report. Neither this report nor any portion hereof may be reprinted, sold, resold, copied, reproduced, distributed, redistributed, published, republished, displayed, posted or

transmitted in any form or media or by any means without the written consent of CLSA and/or CLST. CLSA and/or CLST has/have produced this report for private circulation to professional, institutional and/or wholesale clients only, and may not be distributed to retail investors. The information, opinions and estimates herein are not directed at, or intended for distribution to or use by, any person or entity in any jurisdiction where doing so would be contrary to law or regulation or which would subject CLSA and/or CLST to any additional registration or licensing requirement within such jurisdiction. The information and statistical data (for private or public companies) herein have been obtained from sources we believe to be reliable. Such information has not been independently verified and CLSA and/or CLST makes no representation or warranty as to its fairness, adequacy, accuracy, completeness or correctness. The replication of any third party views in this report should not be treated necessarily as an indication that CLSA and/or CLST agrees with or concurs with such views. None of CLSA and/or CLST, its affiliates and their respective directors, officers, employees, advisers and representatives makes any representation or warranty, express or implied, as to and no reliance should be placed on, the fairness, accuracy, completeness or correctness of such data or information contained herein or any statement made in this report. Any opinions or estimates herein reflect the judgment of CLSA and/or CLST at the date of this report and are subject to change at any time without notice. Where any part of the information, opinions or estimates contained herein reflects the views and opinions of a sales person or a non-analyst, such views and opinions may not correspond to the published view of CLSA and/or CLST. Any price target given in the report may be projected from one or more valuation models and hence any price target may be subject to the inherent risk of the selected model as well as other external risk factors. Where the publication does not contain ratings, the material should not be construed as research but is offered as factual commentary. It is not intended to, nor should it be used to form an investment opinion about the non-rated companies.

This report is for information purposes only and it does not constitute or contain, and should not be considered as an offer or invitation to sell, or any solicitation or invitation of any offer to subscribe for or purchase any securities in any jurisdiction and recipient of this report must make its own independent decisions regarding any securities or financial instruments mentioned herein. This is not intended to provide professional, investment or any other type of advice or recommendation and does not take into account the particular investment objectives, financial situation or needs of individual recipients. Before acting on any information in this report, you should consider whether it is suitable for your particular circumstances and, if appropriate, seek professional advice, including legal or tax advice. Investments involve risks, and investors should exercise prudence and their own judgment in making their investment decisions. The value of any investment or income may go down as well as up, and investors may not get back the full (or any) amount invested. Investments that are denominated in foreign currencies may fluctuate in value as a result of exposure to movements of exchange rate. Past performance is not necessarily a guide to future performance or liquidity. CLSA and/or CLST do/does not accept any responsibility and cannot be held liable for any person's use of or reliance on the information and opinions contained herein. To the extent permitted by applicable securities laws and regulations, CLSA and/or CLST accept(s) no liability whatsoever for any direct or consequential loss arising from the use of this report or its contents.

To maintain the independence and integrity of our research, our Corporate Finance, Sales Trading, Asset Management and Research business lines are distinct from one another. This means that CLSA's Research department is not part of and does not report to CLSA's Corporate Finance department or CLSA's Sales and Trading business. Accordingly, neither the Corporate Finance department nor the Sales and Trading department supervises or controls the activities of CLSA's research analysts. CLSA's research analysts report to the management of the Research department, who in turn report to CLSA's senior management. CLSA has put in place a number of internal controls designed to manage conflicts of interest that may arise as a result of CLSA engaging in Corporate Finance, Sales and Trading, Asset Management and Research activities. Some examples of these controls include: the use of information barriers and other controls designed to ensure that confidential information is only shared on a "need to know" basis and in compliance with CLSA's Chinese Wall policies and procedures; measures designed to ensure that interactions that may occur among CLSA's Research personnel, Corporate Finance, Asset Management, and Sales and Trading personnel, CLSA's financial product issuers and CLSA's research analysts do not compromise the integrity and independence of CLSA's research.

Subject to any applicable laws and regulations at any given time, CLSA, CLST, their respective affiliates, officers, directors or employees may have used the information contained herein before publication and may have positions in, or may from time to time purchase or sell or have a material interest in any of the securities mentioned or related securities, or may currently or in future have or have had a business or financial relationship with, or may provide or have provided corporate finance/capital markets and/or other services to, the entities referred to herein, their advisors and/or any other connected parties. As a result, you should be aware that CLSA and/or CLST and/or their respective affiliates, officers, directors or employees may have one or more conflicts of interest. Regulations or market practice of some jurisdictions/markets prescribe certain disclosures to be made for certain actual, potential or perceived conflicts of interests relating to research reports. Details of the disclosable interest can be found in certain reports as required by the relevant rules and regulation and the full details of conflict of interest with companies under coverage are available at http://www.clsa.com/member/research_disclosures/. Disclosures therein include the position of CLSA and CLST only. Unless specified otherwise, CLSA did not receive any compensation or other benefits from the subject company, covered in this report, or from any third party. If investors have any difficulty accessing this website, please contact webadmin@clsa.com. If you require disclosure information on previous dates, please contact compliance_hk@clsa.com.

Any disputes related to this report shall be governed by the laws of Hong Kong and to the non-exclusive jurisdiction of the courts of Hong Kong in connection with any suite, action or proceeding arising out of or in connection with this material. In the event any of the provisions in these Terms of Use shall be held to be unenforceable, that provision shall be enforced to the maximum extent permissible to reflect the intention underlying the unenforceable term, and the remainder of these General Disclaimer shall be unimpaired.

This report is distributed for and on behalf of CLSA (for research compiled by non-US and non-Taiwan analyst(s)), CLSA Americas, LLC (for research compiled by US analyst(s)) and/or CLST (for research compiled by Taiwan analyst(s)) in Australia by CLSA Australia Pty Ltd (ABN 53 139 992 331/AFSL License No: 350159); in Hong Kong by CLSA Limited (Incorporated in Hong Kong with limited liability); in India by CLSA India Private Limited, (Address: 8/F, Dalamal House, Nariman Point, Mumbai 400021. Tel No: +91-22-66505050. Fax No: +91-22-22840271; CIN: U67120MH1994PLC083118; SEBI Registration No: INZ000001735 as Stock Broker, INM000010619 as Merchant Banker and INH000001113 as Research Analyst; in Indonesia by PT CLSA Sekuritas Indonesia; in Japan by CLSA Securities Japan Co., Ltd.; in Korea by CLSA Securities Korea Ltd.; in Malaysia by CLSA Securities Malaysia Sdn. Bhd.; in the Philippines by CLSA Philippines Inc (a member of Philippine Stock Exchange and Securities Investors Protection Fund); in Singapore by CLSA Singapore Pte Ltd and solely to persons who qualify as an "Institutional Investor", "Accredited Investor" or "Expert Investor" MCI (P) 042/11/2022; in Thailand by CLSA Securities (Thailand) Limited; in Taiwan by CLST (for reports compiled by Taiwan analyst(s) or CLSA (for non Taiwan stock reports to CLSA clients) and in the European Economic Area ('EEA") by CLSA Europe BV and in the United Kingdom by CLSA (UK).

Hong Kong: This research report is distributed by CLSA Limited. This research report is distributed in Hong Kong only to professional investors (as defined in the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) and any rules promulgated thereunder) and may not be distributed to retail investors. Recipients should contact CLSA Limited, Tel: +852 2600 8888 in respect of any matters arising from, or in connection with, the analysis or report.

Australia: CLSA Australia Pty Ltd ("CAPL") (ABN 53 139 992 331/AFS License No: 350159) is regulated by the Australian Securities and Investments Commission ("ASIC") and is a Market Participant of ASX Limited and Cboe Australia Pty Ltd. . This material is issued and distributed by CAPL in Australia to "wholesale clients"

only. This material does not take into account the specific investment objectives, financial situation or particular needs of the recipient. The recipient of this material must not distribute it to any third party without the prior written consent of CAPL. For the purposes of this paragraph the term "wholesale client" has the meaning given in section 761G of the Corporations Act 2001. CAPL's research coverage universe spans listed securities across the ASX All Ordinaries index, securities listed on offshore markets, unlisted issuers and investment products which Research management deem to be relevant to the investor base from time to time. CAPL seeks to cover companies of relevance to its domestic and international investor base across a variety of sectors.

India: CLSA India Private Limited, incorporated in November 1994 provides equity brokerage services (SEBI Registration No: INZ000001735), research services (SEBI Registration No: INH000001113) and merchant banking services (SEBI Registration No.INM000010619) to global institutional investors, pension funds and corporates. CLSA and its associates may have debt holdings in the subject company. Further, CLSA and its associates, in the past 12 months, may have received compensation for non-investment banking services and/or non-securities related services from the subject company. For further details of "associates" of CLSA India please contact Compliance-India@clsa.com. Registration granted by SEBI and certification from NISM in no way guarantee performance of CLSA India Private Limited or provide any assurance of returns to investors. Compliance officer & Grievance officer: Neeta Sanghavi, Tel: 22 6650 5050. Email address of Compliance officer and Grievance cell: compliance-india@clsa.com.

Singapore: This report is distributed in Singapore by CLSA Singapore Pte Ltd to institutional investors, accredited investors or expert investors (each as defined under the Financial Advisers Regulations) only. Singapore recipients should contact CLSA Singapore Pte Ltd, 80 Raffles Place, #18-01, UOB Plaza 1, Singapore 048624, Tel: +65 6416 7888, in respect of any matters arising from, or in connection with, the analysis or report. By virtue of your status as an institutional investor, accredited investor or expert investor, CLSA Singapore Pte Ltd is exempted from complying with certain requirements under the Financial Advisers Act 2001, the Financial Advisers Regulations and the relevant Notices and Guidelines issued thereunder (as disclosed in Part C of the Securities Dealing Services – Singapore Annex of the CLSA terms of business), in respect of any financial advisory services that CLSA Singapore Pte Ltd may provide to you. MCI (P) 042/11/2022.

United States of America: Where any section of the research is compiled by US analyst(s), it is distributed by CLSA Americas, LLC. Where any section is compiled by non-US analyst(s), it is distributed into the United States by CLSA (except CLSA Americas, LLC) solely to persons who qualify as "Major US Institutional Investors" as defined in Rule 15a-6 under the Securities and Exchange Act of 1934 and who deal with CLSA Americas, LLC. However, the delivery of this research report to any person in the United States shall not be deemed a recommendation to effect any transactions in the securities discussed herein or an endorsement of any opinion expressed herein. Any recipient of this research in the United States wishing to effect a transaction in any security mentioned herein should do so by contacting CLSA Americas, LLC.

The United Kingdom: This document is a marketing communication. It has not been prepared in accordance with the legal requirements designed to promote the independence of investment research, and is not subject to any prohibition on dealing ahead of the dissemination of investment research. The document is disseminated in the UK by CLSA (UK) and directed at persons having professional experience in matters relating to investments, as defined in the relevant applicable local regulations. Any investment activity to which it relates is only available to such persons. If you do not have professional experience in matters relating to investments you should not rely on this document. Where research material is compiled by UK analyst(s), it is produced and disseminated by CLSA (UK). For the purposes of the Financial Conduct Rules in the UK such material is prepared and intended as substantive research material. CLSA (UK) is authorised and regulated by the Financial Conduct Authority.

The European Economic Area ('EEA"): research is distributed by CLSA Europe BV, authorised and regulated by the Netherlands Authority for Financial Markets.

CLSA Securities Malaysia Sdn. Bhd (CLSA Malaysia)'s research coverage universe spans listed securities across the FBM KLCI Index, securities listed on offshore markets, unlisted issuers and investment products which Research management deem to be relevant to the investor base from time to time. CLSA Malaysia seeks to cover companies of relevance to its domestic and international investor base across a variety of sectors.

For all other jurisdiction-specific disclaimers please refer to https://www.clsa.com/disclaimer.html. The analysts/contributors to this report may be employed by any relevant CLSA entity or CLST, which is different from the entity that distributes the report in the respective jurisdictions.© 2024 CLSA and/or CL Securities Taiwan Co., Ltd. ("CLST").

Investment in securities market are subject to market risks. Read all the related documents carefully before investing.

Asian Corporate Governance Association
18th Floor, Wilson House
19-27 Wyndham Street
Central, Hong Kong

+852 2160 1788 | www.acga-asia.org